

The energy power game of the European Commission

Neofunctionalism and European energy policy integration

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Preface

This thesis concludes my second master's degree. My degree in European Public Affairs at the Maastricht University inspired me to further pursue EU studies. The master's thesis at the University of Oslo provides an excellent opportunity to do a thorough study in the political science field. This allowed me to combine my interest for the EU integration process and energy policy. I feel privileged to have been able to do such an in depth analysis.

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Abbreviations

CFSP: Common Foreign and Security Policy

CIS: Commonwealth of Independent States

DG: Directorate-General

DG RELEX: External Relations Directorate-General

EC Treaty: Treaty Establishing the European Community

ECSC: European Coal and Steel Community

EEC: European Economic Community

EJC: European Court of Justice

EPE: Energy Policy for Europe

ETS: Emissions Trading Scheme

GS/HS: General Secretariat and High Representative of the European Council

ISO: Independent System Operator

MLG: Multi-level governance

NAFTA: North American Free Trade Agreement

NI: New Institutionalism

SEA: Single European Act

TPA: Third Party Access

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1. Introduction

The EU is faced with multiple challenges in the energy sector. Along with the ongoing efforts to liberalise the energy market, the EU is challenged by a geo-political dependency problem towards Russia, and the very serious threat of global warming. The European Commission has taken the lead in this process to create a comprehensive approach to tackle these challenges. Ernst B. Haas' (1958) seminal work "The Uniting of Europe" introduced neofunctionalism as a theoretical tool to assess integration in Europe. "Spillover" and "loyalty shift" are two central terms in this approach. Spillover is the process of expansion of EU competences, and loyalty shift is used to illustrate how interest groups and decision makers turn their political expectations to the new level of governance (Rosamond 2000: 59-68). With these terms guiding the analysis, I argue that the European Commission is a driver of integration in the energy sector.

This development will be analysed in two stages using different cases. The first case analyses the development of an Internal Market¹ for energy, culminating in the debate over the 2007 3rd liberalisation package on energy markets.²³ I show how the Commission has been successful in using a method of "concession and proposal" to create a political spillover effects to expand EU competencies in energy markets. Furthermore, this case evaluates the degree of loyalty shifts among German stakeholders by analysing reasons for opposition and historical changes in the perception of EU energy policy. The second case provides the context for the Energy

¹ I consistently use the word Internal Market, in which internal energy considerations are treated. Other studies and documents also refer to this as the "Common Market" or the "Single Market", which are the same.

² The proposal is called *the 3rd legislative package on electricity and gas markets* and was issued in September 2007. From here on I will refer to it as the Energy Package.

³ The proposals include: Amending Directive 2003/54/EC concerning common rules for the Internal Market in electricity, amending Directive 2003/55/EC concerning common rules for the Internal Market in natural gas, Regulation establishing an Agency for the cooperation of Energy Regulators, amending Regulation (EC) No 1228/ 2003 (on cross-border trade in electricity), amending Regulation (EC) No 1775/ 2005 (on access to gas transmission systems).

Policy for Europe (EPE).⁴ Here, the Commission induce political spillover and loyalty shift to the external dimension of energy policy by using issue linkage between climate change, the Internal Market and supply security. The last chapter evaluate the neofunctionalist approach to integration using contemporary theoretical contributions to EU studies. The evidence for loyalty shift and spillover in the energy sector is modified by persisting national constraints and evidence of multi-level political orientations. Furthermore, the political spillover process could not be possible without favourable external circumstances.

1.1 Analytical design

European Union politics is studied with a myriad of theoretical approaches. The initial studies of the European project were mainly confined to the “grand theoretical” debate between neofunctionalist, such as Ernst B. Haas and integrogovernmentalists such as Stanley Hoffman and Andrew Moravcsik (Rosamond 2000: 98-113). This debate focused on the actors, trying to establish if it is the supranational institutions or the member states that forge integrative outcomes. This debate is modified in the current debate, as the “governance turn” in the 1990s shifted focus towards the EU as a *sui generis* political system. The study of integration in a grand theoretical scheme was to an extent exchanged for sector studies of political processes. The “old” debate about integration was not rendered obsolete. Rather, research was increasingly focused on using only parts of the classical theories to look at integrative devolvment in policy sectors. In addition, “middle range” theories such as multi-level governance and new institutionalism focused on the complexity of EU decision making and internal factors of national and supranational institutions (Rosamond 2007: 128-135). This study will try to establish how the classical debate over European integration can be combined with contemporary approaches. Being a sector specific study, the

⁴ Energy Policy for Europe (EPE) is the official term used by the EU to describe the coherent approach to energy policy, encompassing environment, energy security and Internal Market aspects of this policy sector. For the rest of the thesis it will mainly be referred to as only EPE

findings will not represent a “grand theoretical” scheme of European integration. The aim is to establish the role of the Commission as an integration driver for energy policy, and neofunctionalism is a coherent framework for assessing evidence for this. Still, with I find it imperative to apply contemporary approaches that can deal with the complexity of EU decision making.

The theoretical starting point is Ernst B. Haas’ seminal work from 1958, “The uniting of Europe”. Haas studied the development towards a federal Europe, and saw the European Coal and Steel Community (ECSC) as a first step in this direction (Haas 1958: Preface). Obviously, the ECSC of 1952-57 was a very modest step towards full European integration. Still, it created the institutions that basically are the same in the present day EU system. Haas established an approach to study the development of Community integration, assessing the degree and origin of political expectations to the Community level. (Schmitter 2005: 255-60). In this study this approach will be applied to the contemporary setting. To assess this, the thesis will provide the historical background of Commission competencies in the energy sector, and how it has gained influence over the last two decades. I will then study in detail the two legislative packages on energy and climate change,⁵ and focus on two aspect of this; unbundling⁶ of gas transmission companies and issue linkage. The first case focuses on the Internal Market and how it is established despite strong opposition from Germany. The second case serves to show how the Commission manages to use one set of competencies to gain influence in others, linking Internal Market and climate change to security of supply.

Both cases are interesting from a neofunctionalist perspective. Germany has had a leading role in opposing liberalisation in the energy sector since the beginning of the project (Stern: 1992: 90). Being the largest economy in the EU and having a privately

⁵ The Climate Change Package is explained in: The policy is explained in: Commission (2008): *20 20 by 2020 Europe's climate change opportunity*.

⁶ The term “unbundling” refers to the separation of ownership assets between supply, transport and distribution of gas or electricity.

owned energy sector, the stakes are high for Germany. From a theoretical perspective it would be significant to find evidence of loyalty shift among decision makers and the industry in Germany. The second case is provided as an example of how the Commission is persistently seeking to expand the scope of EU competencies in the energy sector. To this there is a very high risk of external factors contributing. Certainly, the Commission can not control climate change or events leading to higher levels of security considerations.

Neofunctionalism is a process oriented theory, so events should not be studied statically (Rosamond 2005: 247). The process of integration is very fragmented and dependent on several conditions. The power of supranational institutions might decrease dramatically in a short time span. Furthermore, the Energy Package might be completely obsolete within five years, and it was created as a small piece of a chain of integrative steps. For this study it is thus important to note that the empirical examples presented are merely single cases used to highlight important elements of European integration. I do not predict an end goal to this legislative process, and I realise the limits of generalisation posed by the fact that political integration is a fragile process. This is also why I in this study use more of a theory confirming approach. A more generalising study would have to take into account different policy areas and geographical implications.

1.2 Research question

It is important to define “integration” precisely. In this thesis Ernst B. Haas 1958 definition form “The Uniting of Europe” will be guiding the work:

“Political integration is the process whereby political actors in several distinct national settings are persuaded to shift their loyalties, expectations and political activities toward a new centre, whose institutions possess or demand jurisdiction over the pre-existing national states.” (Haas 1958: 16)

This study will not attempt to predict an end goal of European political integration. It rather focuses on the *process* of integration in a specific sector. This is why in this thesis the operational meaning of the definition will not see the national states as pre-existing, but as the legal foundation of the policy at the national level. The last part of the definition can in this thesis be understood as “(.....)*demand jurisdiction over the national level of governance*”

Using this definition of integration the focus of this study is the role of one central institution, the European Commission.⁷ This institution will not only be the centre of attention, but also the example of the “new centre” as stated in the definition. I therefore to a large extent exclude all other EU institutions, including the European Council, The European Parliament and the European Court of Justice. These institutions are all very important actors in promoting integration, in different ways. I do not claim that the Commission is solely responsible for the process of integration, only that the focus of this thesis is the Commission as an integration driver.

Haas made a three step approach to address questions about the process of political integration. Firstly, one should look at the initial positions of key interest groups and member states. Is this position towards integration in a policy field motivated by economic viability, political expectations or national interest? Secondly, one should ask if the central institutions have created an actual shift in the position towards integration among interest groups and governments, shifting loyalties, expectations and political activities to the central level. Are these shifts correlated with the initial expectations? In this step it must be stated whether the new loyalties, expectations and political activity are created at the national level or by the new institutions. Thirdly, one should examine periodically whether these conditions have been realised, using the above mentioned criteria (Haas 1958: 15-16). All these steps will be examined in this study. The historical background of EU energy policy will identify shifts in the position towards integration. Community legislation in the post- Single European Act

⁷ From here on understood simply as “the Commission.”

Era will be used to show the interaction between the Commission, interest groups and national governments in forging a European wide energy policy. The third step will be shown by the 2007 Energy Package and the EPE proposals as a study of a periodical review of Haas' conditions. Having these questions as well as the revised definition of political integration in mind, the research question of this thesis is:

“How and why has the European Commission gained competencies in the energy sector, despite member state resistance and a limited legal basis?”

This research question needs a few clarifications. Competencies will be defined as “The quality or condition of being legally qualified to perform an act”.⁸ I understand “legal basis” as the explicit written recognition for Community action in a given policy area. These are not contradictory. Limited legal basis is in this study understood as the lack of lack of competencies in the energy sector. In liberalisation of the energy market, the Commission had no competencies in the Treaties until the Lisbon Treaty. However, it did have a legal basis in related policy areas and have used those to achieve competencies also in the energy sector. In the case of the internal energy market it has used competition policy as a legal basis (Matlary 1998: 119-124). Related to the external dimension the EU treaties largely hold security of supplies as a national area of decision making. Still, the Commission does have competencies for legislation in environmental policy as well as a coordinating role of solidarity mechanisms for security of supply.⁹ Thus, the development of competencies has now given the Commission a legal basis in most areas of the energy sector.¹⁰ The use of related policy areas to achieve competencies in the energy sector is central to this study.

⁸ The American Heritage Dictionary of the English Language: <http://www.thefreedictionary.com/competence>

⁹ Haghighi (2007: 103-181) discuss EU competencies in the internal energy dimension of security of supplies, for example the obligation to hold oil stocks. Environmental policy will be discussed in chapter 5 of this study.

¹⁰ That is if the Lisbon Treaty is ratified.

The second clarification relate to “the energy sector”. Here, this predominately relates to the gas market, and except brief mentioning of the closely related electricity market, other sources of energy remain largely unaccounted for. It is important also to note that this is not a study of energy markets, but rather a study of the role of the Commission. That is why the general linkage policy of climate change, security of supplies and the Internal Market will be studied as a phenomenon, rather than a market analysis. In the case of unbundling of vertically integrated companies the study of Germany will relate only to the gas market.

The third clarification relates to the notion of “member state resistance” relates to Haas’ prediction of opposition to shift in political expectations towards the central level. Following Haas, I find it very important to study the resistance of a central member state towards a centralisation of policy making in Europe (Haas 1958: 15-16). The proposal of the Commission to dissolve vertically integrated companies¹¹ serves as an example of a contentious issue which Germany, among other member states, strongly resists. It is important to note that Germany does not directly oppose the issue linkage of the Commission on climate change, energy security and the Internal Market, so this aspect of the research question will be considered separately.

1.3 Research Method

To control for spurious effects, external effects on integration also needs to be assessed, as well as the cost and benefit of integration for member states (Yin 2003: 36). The use of two single cases will contribute to the theory more than using just one, especially if the findings are somewhat comparable (Yin 2003: 51-55). This is the reason why the last part of the analysis will be dedicated to comparing results from the two cases, to see if both can be used to support for neofunctional predictions.

¹¹ To clarify: A vertically integrated company owns the whole infrastructure from supply via transmission to the distribution of gas. An example of this is EON Ruhrgas, which is one of the largest energy companies in Europe.

This methodological approach can be labelled a “theory confirming” comparative case study (Lijphart 1971: 691-3). The purpose of the study is to use established generalisations to analyse theoretical predictions, confirming or infirming these predictions with empirical findings (Lijphart: 1971: 692). Still, the cases are chosen inductively, using established theory to explain the empirical context (Andersen 2005: 97). This makes it theoretically less ambitious than “hypothesis generating” approaches as there will be no attempt to establish new explanations (Lijphart 1971: 692). Comparison between the two cases will be based on two of the central theoretical presumptions in neofunctional theory; loyalty shift and spillover. There are two central problems related to generalisation of the findings. The first problem is that it is impossible to measure statistical variance. I can not say with any certainty that the same findings apply to other cases (Hellevik 2002: 372-373). The strength of this approach is that it is possible to explain in detail how the event under study occurred, rather than the statistical likeliness (Andersen 2005: 137-138). The other problem with the approach is that it must be assumed that there are many cases that can be confirmative to the theory. This means that one more case that fall into this pattern makes little difference for generalisation (Lijphart 1971: 692). Still, it is beyond the scope of this study to improve the level of generalisation of the theory. It rather seeks to use the theoretical framework to better see the context of the unique empirical material. This way, the study will not compare different theoretical assumptions, but rather discuss the strengths and weaknesses of the theory itself. Thus, alternative explanations will also be discussed when analysing the empirical findings. There are also some weaknesses inherent in the neofunctional theory itself, which will be discussed in the next chapter.

There are some considerations that should be noted on the validity and reliability of this study. Regarding internal validity, it is impossible to eliminate alternative explanations to my findings (Yin 2003: 36). In stead, I will try to highlight some of the main challenges to the theory when it comes to externalities in the empirical context. The problem of external validity or generalisation is also a difficult question to address in this study. The theoretical predictions will be subjected to analytical

generalisation (Yin 2003: 31-33). The analysis is based on the theoretical predictions, and they will be subjected to rival explanations (Yin 2003:111- 113). Furthermore, when comparing cases, similarities between them will be assessed. This is a way to replicate the findings to look for explanations that would strengthen or weaken the theoretical assumptions (Yin 2003: 46-8). In this study both cases will assess evidence of spillover and loyalty shifts to explain the enhanced role of the Commission in dealing with energy policy. However, it is a challenge that it is difficult to predict how these conclusions would stick to another case study. To do this it is necessary to conduct further research to assess whether the theory holds in numerous cases (Yin 2003: 37). The reliability question relates to the structure of the data. The data is mainly collected using interviews, and these are anonymous. The reason for this is that the topics discussed are very sensitive, especially regarding the Energy Package. The Commission has been conducting infringement procedures against certain companies in Germany parallel to the discussions about the legislative proposals. This makes the involved stakeholder cautious to say anything publicly that could affect the ongoing negotiations or infringement procedures. However, I do have the transcripts from the interviews ready for inspection by the Department of Political Science at the University of Oslo to control the data if necessary.

There are some important implications using interviews for both the validity and reliability of the study. The validity is increased by drawing on different sources of data (Yin 2003: 98-101). This is why I rely on interviews as an important supplement to using other written primary and secondary sources. Talking to the people involved directly in the process gives a very valuable first handed insight into the decision making process in Brussels. By talking to different stakeholders it is possible to detect the conflicting interests and biases. The latter is a notion that affects the reliability, because if another investigator asks the same questions to the same people in five years the result might be different (Yin 2003: 37-39). This relates heavily to the context of the study. There is at the moment a harsh climate in Brussels about the Energy Package. There are conflicts of interests and there were some extraordinary events surrounding it. Right before I went on the fieldtrip for this study, E.ON

Ruhrgas made an announcement going against its own government, spreading uncertainty among stakeholders.¹² This is why you can easily get the impression that they are saying what they want you to hear to avoid disturbance. By looking at opposing views, bias can be detected. It is also helpful to identify a few distinctive tensions to tag the discussion on and to identify alternative explanations.

The interviews were not selected at random. I conducted all interviews in Brussels from 3-7 March 2008, 7 in person and two by telephone. The selection was made in a combination of requests from the author and self-selection. All of the interviews were chosen after some guidance from contacts already working in the field of expertise. Some interviews were arranged directly, while in other instances institutions have gotten a more broad invitation based on their knowledge and they have selected an appropriate candidate. The interviewees talk on behalf of themselves and who they represent. It is not possible to draw the conclusion whether what they say represents whole organisations, and that was not the purpose either. Rather than having statements similar to those already published, I wished to have an open discussion about the issues at stakes and this was largely well accomplished. The questions were open, even though I had an interview guide with me. All except two interviews were taped and transcribed. Since there is a fear of the interviewees being too personal, and thus less representative, I relied on more than one source representing each “side” in the debate. There were in total nine interviews and one written reply. The EU side were represented with five people divided among the Commission, Council and European Parliament. The German side were also represented with five responses including the written reply. These were from the German government and gas industry, including peak associations and individual companies. By relying on a variety of interviews in combination with other primary and secondary sources it is my belief that the validity and reliability is sufficient to claim an analytical contribution to the theory. The problem of generalisation derived

¹² For more about this decision see Euractiv 29.8. 2008: <http://www.euractiv.com/en/energy/eon-surprise-grid-offer-bolsters-eu-liberalisation-hopes/article-170630>

from this kind of a study is to an extent remedied by applying the same theoretical framework in two different cases. Still, I recommend further case studying with the same theoretical framework to enhance the level of analytical generalisation (Yin 2003: 37). This framework is the subject of the next chapter.

2. Neofunctionalism

European governance is a mix of highly intricate decision making procedures, and the nature of cooperation varies across the different policy areas covered (Rosamond 2007: 128-129). The task of this study is to explain why the Commission gained influence in the energy sector, despite the fact that several member states have been very reluctant to admit these competencies to supranational level. It is a fact that the level of integration in the energy sector has been ascended, especially in the two last decades. Integration theory will be the starting point in the analysis of why a member state would transfer sovereignty to a supranational body. Neofunctionalism is one of the main theories of European integration, and will shed light over integrative developments.

Neofunctionalism is one of the main scientific paradigms for understanding the EU integration process (Rosamond 2000: 50-51). The theory evolved in the harsh scholarly environment after World War II, when idealism was stated to be a dead theory. In political science, realism was the sober approach to international relations (Ruggie et al 2005: 273). The US political scientist Ernst B. Haas was born and raised in Germany, but fled to USA in 1938. When he returned to Europe, the integrative potential of the Paris Treaty in 1951¹³ soon caught his attention. Inspired by the EU “founding fathers” Robert Schuman and Jean Claude Monnet¹⁴, he presented a new way of looking at international cooperation (Ruggie et al 2005: 278-9). Because of the innovative nature of the theory he had to assure his fellow international relations (IR) scholars that the approach had no idealism entrenched. In fact, neofunctionalism shares quite a few traits with realism, especially the self interest oriented approach of both scholarly positions (Rosamond 2005: 238- 2).

¹³ The treaty established the European Coal and Steel Community (ECSC), the predecessor of the EEC, EC and EU.

¹⁴ Robert Schuman made the “founding document” of European integration. 9. May 1950 the Schuman Declaration was proclaimed, and the day is now celebrated as the “national day” of the EU.

Ernst B. Haas did not perceive neofunctionalism as a theory, but rather as an integrative process (Ruggie et al 2005: 275).¹⁵ His approach was very empirical, and studied the evolving and expanding technocratic governance in the supranational High Authority, as well as the process of loyalty shifts towards the other ECSC institutions (Ruggie et. al 2005: 277-281). The technocratic focus of his work highlighted his inspiration from David Mitrany and Max Weber. David Mitrany was an inter war functionalist, who emphasised the growing technocratic governance in bureaucratic organisations. This is not unlike Max Webers ideal type bureaucrats making assumptions about modern governance (Rosamond 2005: 239-40). However, Haas split with functionalists with the agency approach of neofunctionalism, suggesting ample space for the manoeuvring of self- interested actors in supranational institutions (Rosamond 2000: 55). Part of the explanation why these supranational actors became influential can be found in the shift of loyalty among member states and interest groups.

2.1 Loyalty shifts

One of the basic assumptions of neofunctionalism is that the advent of new regional institutions creates shifts in loyalty from the national level to the new regional centre (Rosamond 2000: 65-68). Haas defined political loyalty as:

“A population may be said to be loyal to a set of symbols and institutions when it habitually and predictably over long periods obey the injunctions of their authority and turns to them for the satisfaction of important expectations” (Haas 1958: 5)

This happens in several phases. To begin with, national states voluntarily agree to transfer authority in specific policy areas to the new level of government (Ruggie et. al 2005: 278-9). In the establishing phase of new central institutions, the incumbents

¹⁵ His two main contribution to neofunctionalism are “The Uniting of Europe: Political, Social and Economic Forces, 1950-1957”(1958) and “beyond the Nation State: Functionalism and International Organizations” (1964)

will start their work with a national bias. This was certainly the case with the High Authority of the ECSC in the founding years, where national interests prevailed, and the representatives followed a narrow interpretation of the Treaty obligations (Haas 1958: 451-486). As time passes, the institutions establish an “ideology” of their own. This was also the case in Haas’ studies, where the High Authority followed a more progressive path in the last year, less eager to ease the will of member states (ibid). As institutions after a while start to operate with distinctive traits, values shaped in the institutions affect the member states. Interest groups and politicians at the national level will get expectations of policy making at the EU level (Jensen 2007: 91-92). These expectations could be positive or negative, depending on the nature of the policy area and actors involved, but the result is that politicians and interest groups address these expectations at the central level (Haas 1958: 13-16). This way there has in fact been a shift of political loyalties, as defined by Haas, to the supranational level. This could be seen as a simplified prediction that fails to capture the highly complex nature of pluralist society, in which loyalties can rest at different levels at different times (Rosamond 2000: 65-68). Furthermore, the notion of European loyalties was challenged by the presence of strong characters such as Charles de Gaulle (Ibid). The French president seriously halted European integration in the 1960s, introducing more majority voting and thus intergovernmental behaviour in the EU. With these considerations in mind, the transfer of loyalty and expectations will serve as a basic assumption in the study of the present day Commission. These loyalty transfers not only serve to establish new centres of decision making but also to create spillover effects of policy areas to be covered.

2.2 Spillover

Early Neofunctionalism predicted European integration as a result of automatic spillover of competencies, rather than national surrendering of power through interstate bargains (Rosamond 2000: 59-61). The latter approach is the prominence of intergovernmentalism¹⁶. Haas had difficulties to see the state as an actor with one single interest, and neofunctionalism is thus very much inclined towards social pluralism (Rosamond 2005: 239-41). Integration starts with giving authority to a supranational body in one sector. Integration in one policy area will lead to a realisation that an expansion of tasks covered by the supranational authority is needed to achieve the original policy goals (Ruggie et al 2005: 279).¹⁷ This is because problems in one sector can not be remedied without similar action in related sectors (Rosamond 2000: 60). Furthermore, different societal groups will peak their interests and approach the new level for support (Rosamond 2005: 243-4). This will create pressure from interest groups to integrate politically, because they want to influence policy at the highest level possible (Rosamond 2000: 62-63). This shift in loyalty for interest groups and decision makers reinforces their commitment to the supranational authority¹⁸ (Haas 1958: 9-11). The result is a cognitive preference for the supranational level among policy makers following an expansive logic (Rosamond 2005: 244). The process can be explained this way:

¹⁶ Andrew Moravcsik is the most prominent intergovernmentalist scholars. This discipline views integration as a series of interstate bargains between rational and coherent states, acting out of self interests. For an example see: Moravcsik (2005): *"The European constitutional legacy and the neofunctionalist legacy"*

¹⁷ More contemporary neofunctionalists would be able to see this mechanism in the case of the economic cooperation in Europe, and how it evolved from barriers to trade to a common currency through more intervened needs (Rosamond 2000: 60).

¹⁸ It is worth noting that this does not require a shift in loyalty of the masses, only the actors involved. It is thus not expected that loyalties of people in general would shift from the nation state to the EU (Haas 1958: 16-19).

“Spillover refers...to the process whereby members of an integrative scheme – agreed on some collective goals for a variety of motives, but unequally satisfied with their attainment of these goals – attempt to resolve their dissatisfaction by resorting to collaboration in another, related sector (expanding the scope of mutual commitment) or by intensifying their commitment to the original sector (increasing the level of mutual commitment), or both”. (Schmitter 1969: 162)¹⁹

The concept of automatic spillover has been criticised, because of recurrent setbacks and time lags in the integration project (Jensen 2007: 93-95). An alternative to this functional way of looking at spillover is that of “guided” or “political” spillover by supranational actors such as the Commission (Jensen 2007: 90-91). Firstly, the supranational institution may use the agenda setting power to pave the way for integrative solutions even in the face of member state resistance. Secondly, the Commission often piles together legislative proposals in package deals to make it difficult for single members to resist. Thirdly, the Commission can use its brokering position to achieve common goals (Ibid). Also, as discussed, interest groups and decision makers might wish to enhance cooperation by conceding competencies in perceived self interest. The end result is that the supranational authority can work as a driver of integration, using its power of agenda setting as well as the shift of loyalties and expectations to achieve more integration (Rosamond 2000: 61). Another approach to decouple the idea of spillover from automaticity is to examine the role of externalities. These can either help or hamper integration approach depending on the distribution of benefits, external threats and costs of integration (Rosamond 2000: 72). Only if these conditions are perceived as favourable integration can be set off. In addition, these conditions could potentially also explain developments outside Europe (Ibid).

¹⁹ in Jensen (2007: 90)

2.3 Theoretical limits

Historically, the nationalism of French president Charles de Gaulle posed a tremendous challenge to students of neofunctionalism. His lukewarm attitudes towards European integration was by most scientists seen as a proof that neofunctionalism failed to take into account the influence of national sentiments and strong actors in the political system (Rosamond 2000: 67). Even Haas published a paper in 1975 that is seen as the mortuary of neofunctionalism.²⁰ The theory needed to deal with the fact that consensus between economic elites and political actors in the nation states is in fact a fragile basis for integration. Conflict is the driver of pluralist societies, and pure technocratic governance will have difficulties in balancing these conflicting goals in the presence of strong political figures and nationalism (Rosamond 2000: 67-68). These concerns made the theory unapproachable for several years, but neofunctionalism had a revival in the 1980s (Ruggie et al 2005: 280). The Single European Act (SEA) sparked an ongoing and unprecedented integration process in Europe. In the post SEA- era there are several developments to be noted. Firstly, externalities such as neoliberalism and international economic trends have played a crucial role in creating economic interdependencies in Europe. Secondly, member states have played a vital role in forging the EU Treaties. Thirdly, there is still a low level of public participation in the EU process (Schmitter 2005: 261-2). Still, the focus on log rolling and package deals in the EU system seems to create irreversible interdependency among EU actors (Schmitter 2005: 266). Furthermore, the contribution of European institutions in catalysing integration and strengthen the role of EU law in member states is significant (Schmitter 2005: 261-2). Therefore, after its recovery from demise, neofunctionalism is a theoretical approach that can not easily be ignored in studies of the EU (Rosamond 2000: 50).

A very significant challenge to neofunctionalism is that it is apparently limited to Europe. This indicates that neofunctionalism is more a descriptive exercise than a

²⁰ Ernst B. Haas (1975): "The Obsolescence of Regional Integration Theory"

theoretical approach (Rosamond 2003: 69). Haas and Schmitter (1964) countered this by saying that context is not irrelevant (Rosamond 2000: 71). The EU countries are plural societies with a tradition of confining conflict to institutional settings. Also in other regions integration and spillover would be expected if economic, social and political conditions are in place. This would accommodate a process of merging technocratic and economic goals (Rosamond 2003: 71-73). However, this is still one of the most contentious issues in neofunctionalism, because the theory is apparently not robust enough to explain the lack of political integration in other plural societies, for instance with the NAFTA agreement in North America (Rosamond 2000: 68-72). It is also difficult to predict if the theory is applicable to other regional settings with the background variables in place, since there are no empirical examples of similarly ambitious political organisations in Africa, Asia or South America. I will not go into any more details about this theoretical limit to neofunctionalism other than stating that it is a challenge to be noted.

Another important element in the integration process is the distinction between high and low politics. In neofunctional reasoning it is common to see integration as something that happens most prominently in low politics. It is easier for political actors to concede authority to the supranational level in the economic area than in vital national security questions (Rosamond 2000: 51-52). In an attempt to explain the integrative gap between integration in “high” and “low” politicisation, Börzel (2005) studied the integration in all sectors of EU policy making, and separated between level and scope of EU competencies to better understand the pace of EU integration in the different policy areas. “Level” refers to the place in which competencies lie. “Scope”, on the other hand, refers to the procedures in which decisions are made; from purely supranational decisions, to purely inter state bargains (Börzel 2005: 219-22). By studying all the Treaties it is possible to trace the integrative development of the EU, differentiating between level and scope. If considering EU foreign energy policy as a part of the political external relations dimension, Börzel would find that there have in fact been an integrative move, mostly in level (Börzel 2005: 222). On a scale from 0-5 in integration, external relations have moved from 1 in level and 0 in

scope, to 3 in level and 2 in scope.²¹ This means that with the proposed Constitution Treaty in 2004²² there has been a split in competencies between national and EU level in CFSP, and legislation would be made with intergovernmental cooperation (Börzel 2005: 221). These finding shows that the integration process is by no means strictly limited to economic attributes. At the same time it is also a reminder that “high politics” offer challenges for students of neofunctionalism, because these policy areas seem to be more vulnerable to external pressure and political competition at the national level (Börzel 2005: 231).

2.4 The governance turn

Regional integration theories have been refined in many ways since Ernst B. Haas declared neofunctionalism dead in 1975.²³ In the 1990s EU studies experienced a governance turn, shifting the focus from integration to the sui generis nature of EU governance. These theories refuse to see European integration solely through a neofunctionalist or intergovernmental perspective. In stead of creating “grand theories” these approaches were created as middle range theories that seeks to explain specific developments within different policy sectors (Rosamond 2000: 105-113). Multi-level governance, new institutionalism and differentiated integration are among the most important theoretical frameworks that have been developed.²⁴

²¹ In the same study, Börzel identified integration in the internal energy market to have gone from 1,5 in level and 2 in scope to 3,5 in level and 4 in scope.

²² Börzel uses the Constitution Treaty as the last Treaty of study. This Treaty was never ratified, so a similar study of the proposed Treaty of Lisbon would be needed to assess this properly. Still, the agreement between Heads of States for Treaty revision shows the intent to further integrate. For a full account of the amendments to the Lisbon Treaty see: CIG 14/07: <http://www.consilium.europa.eu/uedocs/cmsUpload/cg00014.en07.pdf>

²³ Haas (1975): “The Obsolescence of Regional Integration Theory” is one of the most interesting self inflicted theoretical mortuaries in political science.

²⁴ These are the approaches that will be used for this purpose. This way the study will cover the issue of multiple jurisdictions and institutional constraints in the Commission. In addition it looks at how national implementation of EU policy matters. In addition to those mentioned here, contemporary EU theories also include various actor- based and policy network models (Rosamond 2000: 123-6). These will not be covered here, as I am not intending to provide an exhaustive list of theories, rather show the complexity of EU decision making that challenges neofunctionalism.

MLG captures the *sui generis* nature of European integration, without losing track of the nation state.²⁵ The theory predicts that organisations and policy makers accept that there are at least two tiers of decision making for interest groups within the EU system. This way, MLG acknowledges the complexity of EU decision making (Rosamond 2007: 128-9). There are several ways of looking at this. Firstly, decision makers and governments approach more than one level to influence decision making. Secondly, functional tasks seldom overlap geographical borders. The overlapping geographic structure of political actors and functional tasks makes it difficult to impose one level of governance on each policy area (Rosamond 2000: 110-13). Rather, they remain tangled up in multiple jurisdictions and loyalties, adding to the complexity of EU decision making. This relates to the third issue, that the EU is not a federal state and can not provide overlapping functional jurisdictions (Hooghe, Marks 2003: 8-9). In stead the EU must rely on sector specific arrangements in areas which are sensitive to national security (Junge 2007: 392-5). It is possible to argue that this hampers the idea of having an encompassing energy policy because the EU must separate policy areas to avoid infringing on the right of member states to control externalities. These considerations are clear modification of neofunctionalism, which would predict a loyalty transfer from the national to the supranational level. The persisting national constraints have challenged this assumption. Following is an example of how interest groups organise according to resources and capacity when approaching EU decision making.

Inspired by multi-level governance, Rainer Eising (2004) studied how different business groups react to integration. In his quantitative analysis he identified five types of organisations from the EU level, Germany, France and Great Britain in addition to large multi-national firms. The organisations he studied were niche organisations, occasional players, traditionalists (intergovernmentalist assumption), EU players (neofunctionalist assumption) and multi-level players (multi-level

²⁵ For an example see: Hooghe and Marks (2003): *Unravelling the Central State, But How? Types of Multi- Level Governance*.

governance assumption). The main theoretical approaches would only consider the last three organisations, but the occasional players and niche organisations falls outside these theoretical assumptions since they are too small or single issue linked. The main findings supported the notion that different actors seek different levels. Large firms are overwhelmingly multi-level players, while only EU associations are mostly EU players. National associations where on average about a third traditionalistic and the rest were divided quite equally between all other categories, except EU players. Thus, only purely EU peak organisations match the neofunctionalist assumption, while national organisations are more traditionalistic or multi-level players. Whether or not an organisation seeks influence at both levels seems to depend on its organisational capabilities. Large firms have vast resources and issue specific knowledge to seek a dual strategy of influence (Eising 2004). This can be seen as an empirical example of how interest groups hold different allegiances, and change loyalties according to the question at stake and resources involved. Multi-level governance is thus an approach that captures the complexity of interests and access points for the contemporary setting.

Differentiated integration is a theory that tries to combine integration theories with the Europeanization approach (Andersen et al 2006: 315). The latter framework focuses on the how EU policy affect national institutions and vice versa. On the one hand, European norms and systemic characteristics shape national institutions, as they need to adapt to harmonised EU rules. On the other hand, national traits also feed into the EU system creating an interplay between the levels (Quaglia et al: 2007: 406-7). The theory of differentiated integration acknowledges the importance of national constraints and look at how EU legislation is made flexibly to endorse opposing national cultures (Andersen et al 2006: 313-15). Using organisational theory, the approach seeks to examine not only Europeanization of political systems, but also the process of integration. Having in mind the integration process, the approach dismisses the notion that there is a necessarily a normative coupling between the EU and national level. Even if this coupling is tight, there may be ample space for different organisational solutions. In addition, homogenous integration can be hampered by

strong local pressure for decoupling between the national and EU level (Andersen et al 2006: 320-1). These concerns force EU level decision makers to water down policy proposals and allow for more flexibility. The result is various forms of flexible mechanisms such as “concentric circles”, “multi-speed Europe” and “Europe la carte”. Each of these mechanisms is a way of allowing some member states to proceed faster than others in certain policy areas, in the face of persistent member state resistance or lack of resources (Junge 2007: 398).

The last interesting governance perspective applied to this study is that of new institutionalism. This approach brings institutions “back in”, opening for studies of the internal constraints of institutions (Rosamond 2000: 113-14). The approach seeks to look at institutions as an intervening level between actor preferences and policy outputs providing an arena for interaction and information (Ibid). There are several variants of NI theories; the most notable being historical, rationalist and sociological approaches (Rosamond 113-122). These approaches prioritise different aspects of institutional features, be it the historical architecture of the institutions, preferences of actors involved in the shaping outcomes or cultural and organisational practices (Ibid). What combines these approaches is that institutions are carriers of informal rules and norms that shape actor preferences beyond the institution itself (Rosamond 2000: 114). In addition, institutions are made up by different sets of actors that influence each other (Christiansen 1997: 74). The European Commission faces contradictory pulls between politicization and bureaucracy which to a certain extent determine how it relates to different policy areas (Christiansen 1997: 76). As the Commission is the centre of attention in this study, a discussion about potential internal constraints for the Commission will be developed.

2.5 Predictions: The Commission as an integration driver

Based on the theory of Ernst B. Haas, and the subsequent limits and modifications to neofunctionalism, there are a few predictions to be made about the analytical part of this study:

1. I will expect to find a shift in loyalty from interest groups and decision makers in the energy policy area towards the EU institutions, here represented by the Commission. The key task in this respect is to find out how and why these expectations which creates shifts in loyalty are evolving. The empirical findings will be assessed using governance theories as well as Haas' original theory. In this respect I would expect to find evidence of increased coherence towards EU legislation. This means that policy makers and the industry should be thinking more "European" when approaching energy policy. Still, using theories of European governance it should be expected that there are tensions between the Commission as a driver of integration and preferences of national states in specific policy areas. Firstly, there will be a degree of national interpretation of EU legislation, allowed for with flexible mechanisms. Secondly, national level priorities in energy policy making will still be very important in the approach of the member states and industry toward EU policy making. Thirdly, institutional constraints within the Commission must be taken into account, as it can not be expected that the institution is a unified actor in every instance. Institutions may also contain elements of multiple loyalties and normative divergence.
2. The loyalty shift is to a large extent created by the Commission as a result of its drive for integration. National interest groups see the need for cooperation at the supranational level to better solve their problems. The central institutions in turn seek to enhance influence as they gradually take on more responsibility and are able to use its agenda setting power and broker role to enhance integration. This means that it is expected that loyalties are driven from the central level, not the other way around. The reasoning for such a prediction lies

in the value of agenda setting power for the Commission. As the Commission persistently drive for EU level competencies in the energy sector, it would be expected that they in the end succeed in establishing new loyalties. However, it is not expected that these loyalty shifts will be irreversible or exclusive. Ties to the national level remain strong, and member states will still resist certain aspects of integration. Furthermore, the idea of loyalty shifts as driven by the Commission will be somewhat modified by external events, something that also relates to the next prediction about spillover effects.

3. The next prediction would be that there is evidence of spillover effects in the evolution of an Energy Policy for Europe. Following neofunctional reasoning cooperation in one sector will create a shift of loyalty and expectations towards Community action other sectors. This in turn will create increasing interdependencies that calls for cooperation in related sectors. The Internal Market on energy has been developed from being a strictly national policy area to being an integrated part of the Internal Market. To the external energy dimension, the Commission has established a linkage between energy security, climate change and the Internal Market. This is not necessarily created by natural spillover effects. Rather, the Commission politically drive the spillover effect by the active use of issue linkage and a method of proposals and concessions. In fact, the main prediction will be precisely that the activism of the Commission is the main reason why political spillover has occurred. The “energy power game” between the Commission, member states and the industry will be empirically examined to show how these spillover effects unfold. It is expected that within these empirical findings the idea of spillover will be modified both with respect to member state resistance and inter state bargaining. Also, external conditions will probably play a vital role in shaping preferences of member states. External conditions will thus be thoroughly examined in the analytical part. Finally, I expect to find different effects of spillover differentiating between level and scope of EU competencies in both cases. Even if decisions are taken at the EU level there should be different

degree of coherence to EU policy making depending on the national constraints. In both case the energy policy should be less integrated in scope than in level, meaning that member states maintain an important role in energy policy.

In the following section of the thesis, neofunctional assumptions will serve as a guide to the empirical richness of energy decision making. With all the limits posed by neofunctional reasoning mentioned in this section, I am fully aware of the difficulty in generalising from the empirical findings. Still, the agenda setting power of the Commission and the remarkable pace of integration in the energy sector deserves attention from a neofunctionalist perspective. The empirical starting point of the study will be the historical development of EU energy policy.

3. Background of the Energy Policy for Europe (EPE)

At the moment the EU has a coherent approach to the entire scale of energy policy, from the internal to the external dimension, called an Energy Policy for Europe (EPE). In January 2007 the Commission issued a press statement and a leaflet explaining in detail what EPE entails.²⁶ The main features are to have a coherent climate change policy and speak with one voice internationally in energy affairs. In addition it seeks to complete the Internal Market. Even with all its limitations, EPE is an established policy and there is a highly intricate economical and geopolitical backdrop that this policy seeks to manoeuvre in. The history and the evolving rationale for having such a policy will be discussed in detail in this section. Furthermore, there will be a presentation of the geopolitical backdrop of contemporary European supply security questions.

3.1 The Schuman Declaration: A European federation

European integration started with the coal and steel sector, both highly important energy and industry sectors in the early post-war era. However, the problem with coal was that it was losing ground. Several price crises, and frequent coal subsidies were among the features of the coal industry in the 1950s. In addition, German steel makers were running cartels, keeping prices artificially high. Under these conditions, the High Authority supposedly had a great chance to use its Treaty obligations to control the energy sector. This did not by far happen (Haas 1958: 451-86). The Treaty of Paris established the European Coal and Steel Community, which was more than an

²⁶ http://ec.europa.eu/energy/energy_policy/doc/2007_03_02_energy_leaflet_en.pdf

industrial organisation. The Treaty was partly based on the Schuman Declaration of 9 May 1950, a testament of federal ambition:

“ (...)The pooling of coal and steel production should immediately provide for the setting up of common foundations for economic development as a first step in the federation of Europe(...) (...)In this way, there will be realised simply and speedily that fusion of interest which is indispensable to the establishment of a common economic system; it may be the leaven from which may grow a wider and deeper community between countries long opposed to one another by sanguinary divisions (...) (...)The Authority's decisions will be enforceable in France, Germany and other member countries..(....) (Schuman declaration: 1950)²⁷

This way of thinking resembled that of Jean Claude Monnet, a federalist and the first president of the ECSC High Authority (Rosamond 2000: 51-54). Monnet left office after only three years, frustrated by the lack of federal vision among his colleagues (Haas 1958: 273). The Paris Treaty competencies were largely unused by the High Authority, since it applied a very narrow definition of its obligations. It had a liberal merger policy, it never imposed fines, and it did not support radical wage equality measures suggested by the labour unions (Haas 1958: 451- 486). It could be claimed that The High Authority was for the member states and industrial leaders, and at best lukewarm to labour unions with federal ambitions. The effect was that coal subsidies remained high, and steel producers could operate with little intervention (Ibid).

Initially, there was a lack of political will from member states to let Community institutions handle energy policy (Matlary 1998: 12-19). Coal and steel demised in importance to EU countries as oil gained momentum from the 1960s. Forging a common energy policy based on the “old” energy sources was not seen as important or necessary (ibid). Still, the ECSC was seen as a success (Haas 1958: Preface). This was because it managed to pave the way for a common market. And as the High Authority realised this development in the late 1950s, it grew more assertive, and

²⁷ http://europa.eu/abc/symbols/9-may/decl_en.htm

there were already traces of integration demands in other sectors (Haas 1958: 451-486). Thus, the Treaties of Rome, establishing the European Economic Community and European Atomic Energy Community was far more reaching in its Community provisions than was the Treaty of Paris. Integration in the 1950s was not an easy task, and it soon proved to be the case that economic sector with low security considerations would be easier to integrate (Rosamond 2000: 51-52). The ECSC paved way for further integration as common trade rules were established, but the energy sector remained national in level.

The ECSC experience is an ambiguous story of integration and disappointment. It did create loyalties and expectations to the central level, especially within the labour unions (Haas 1958: 465-69). It showed how cooperation can create spillover effects within low policy areas in the EEC agreement (Haas 1958: 301-17). However, in the case of energy, integration failed to take roots. An important reason seems to be that the balance of cost and benefits of energy integration was conceived to be less than positive sum by decision makers. Joseph Nye's (1971) background conditions for political integration seems compelling to explain this development, in which two conditions are necessary to be able to integrate policy sectors, external threats and costs. The industry and member states arranged gas deliveries according to a perceived risk of supply failure strictly balancing supply and demand (Stern 1992: 1-10). So instead of following an integrative path, the energy sector fell in its own tracks, left out of the EEC Treaty.

3.2 National gatekeepers

Energy policy between 1960 and 1990 followed a specific pattern of nationalised ownership (Stern 1998: 10-32). One of the main structural characteristic of the old system was that transmission gas companies had immense power. These companies, like Ruhrgas in Germany and Gasunie in the Netherlands, had the role as national gatekeepers, and the aim was to keep prices high and balance supply and demand (Stern 1998: 13-15). This was done with governmental backup, because they had an interest in supplying gas directly to residential consumers and industrial complexes. This served to avoid using gas in electricity generation, and thus boost the need for coal and nuclear power that in many states could be produced domestically (Stern 1998: 30-32). The consumer lost out on this. As energy distribution in Europe was mostly tied up in local public owned power stations, they were completely dependent on the transmission company in their region.²⁸ In addition, local governments often used high gas prices to subsidise other areas of public service, adding to the unfair pricing of gas (Stern 1998: 19-20). Even though the large industrial complexes received gas with subsidised prices to prevent them from switching to other sources of energy, prices were kept far over the actual price of production. The gas market in Europe could be described as a system with low production costs, high prices and few players (Stern 1998: 28-30). Even when buying gas from major suppliers, the companies got together in consortiums, preventing actual competition (ibid). The national gatekeeper system gradually and forcefully changed in the late 1980s as a result of market liberalisation. This brief overview of European energy policy over three decades is sufficient to show that there was virtually no integration in the energy sector. That is why I will now turn to the Single European Act and subsequent liberalisation efforts.

3.3 Third Party Access²⁹ and member state resistance

In 1988 the Commission issued a working document called “the internal energy market”³⁰, starting the process that lingers on twenty years later. For the Commission, the conditions for integration of energy into the Internal Market had changed with the 1986 Single European Act (Stern 1998: 5-6). The Commission clearly demonstrated this in the 1988 working document calling for application of Community law into free movement of goods, state monopolies, state aid and rules of competition into the whole energy market. The question is how this assertiveness developed. In the history of the EU, the power of the Commission over integrative developments has been highest when there is a momentum for the European project (Matlary 1998: 145). This was certainly the case in the late 1980s, when the process of integration finally took off after years of hampering caused by Charles de Gaulle’s intergovernmentalism. Clearly, the Commission saw the potential because member states had already agreed to enlarge the Internal Market. In addition, external events in Eastern Europe and the Gulf and consequent supply concerns put energy on top of the political agenda (Matlary 1998: 22-23). However, establishing a common energy policy was not an easy path. The energy sector consisted of several powerful actors, not ready to change status quo.

As soon as the 1988 working document was published, the industry prepared for battle. The United Kingdom was one of the few countries to support liberalisation measures, because it had liberalised its own market as early as 1982 (Stern 1992: 70-86). The initial Gas Transit Directive of 1990 was introduced as a first step towards

²⁸ This was especially the case in Germany, where the gas market was organised with “demarcation and concession”. This means that the distribution companies divided the market between them and then made legal agreements with the transmission companies to prevent a change of supplier (Stern 1998: 12).

²⁹ Third Party Access (TPA) is a debated policy option for allowing a company that do not own the pipeline in question to transport its gas through it. This is introduced to enhance competition. For an in depth analyses of this option see: Stern (1992): “Third Party Access in the European Gas Industries”.

³⁰ “The Internal Energy Market” COM (1988) 238 final

liberalisation and received such opposition that the Commission was forced to note in the Council Minutes:

*“The Commission states that the sole objective of this Directive is to facilitate Transit (...) and could not in any circumstances be interpreted as a legal basis for allowing free access to grids. (...) The Council notes that strong opposition exists within it (...) The Commission will take full account of this situation.”*³¹

The Transit Directive passed in a last minute compromise, but this could only happen because it implied modest changes, related to third country transit and not directly at national gas transmission (Stern 1992: 70-71). The real contentious issue was that of third party access (TPA), which would force companies to open the full spectre of the gas pipeline infrastructure to competition. By 1991 it was clear that the Commission wanted serious measures of liberalisation, including TPA, abolition of privileged companies and unbundling of transmission from distribution. This would happen in a three stage approach, stage one being the Transit and Price Transparency Directives. The second stage would be the Directive on Common Rules on energy markets, including unbundling of the accounting division in transmission companies from distribution. Stage three would entail further liberalisation, including TPA starting from 1996 (Stern 1992: 63). To do this, the Commission tried to repeat the success of competition regulation in the telecommunication sector, notably by using art. 90 of the EC Treaty. This would make it possible for the Commission to force *member states* to abandon energy monopolies in stead of obliging the industry to liberalise, which would be the case using the competition article, 100a. Central member states and the industry were shocked. It soon became clear that the member states would not dissolve their large and often fully state owned companies. Therefore the Commission proposed measures based on competition rules to introduce full scale liberalisation (Stern 1992: 58-69). This was more acceptable, but as it became clear that the industry

³¹ Stern (1992: 73)

and the member states would give the Commission a hard time to liberalise the gas market, the focus shifted temporarily to the electricity sector (Stern 1998: 91-94).

The Directive for Common rules in the electricity market entered into force in 1996.³² This was an important step for the Commission, because it paved way for the gas sector. TPA requirements in the electricity sector did not come easy, and the French negotiators managed to apply its own proposal of international electricity sale requirements, the “single buyer approach”. This would let countries chose to either open the market for TPA or organise all international sales through the government. This was a very limited agreement, which upheld the status quo for the French state owned utility structure (Stern 1998: 92-93). After four years of negotiations the Commission was able to set a precedent in the electricity sector. After Conceding to the French proposal it was at least easier for large industrial users to switch suppliers, and TPA was given equal status as “the single buyer” approach (Ibid). With this decision in place the gas market was next on the list.

3.4 The completion of the Internal Market

In 1998 the gas market directive was finally agreed upon. This was the result of two years of bargaining between the Commission and central member states over TPA requirements (Stern 1998: 94-98). The deal provided for the gradual introduction of TPA, but there were severe limitations to liberalisation. The most important aspect related to the lack of regulation (Stern 1998: 100-102). There was no actual provisions of how to monitor TPA, the only mentioning of this was:

³² Directive Concerning Common Rules for the Internal Market in Electricity. 96/92 EC

“Member states shall create appropriate and efficient mechanisms for regulation, control and transparency so as to avoid any abuse of a dominant position, in particular to the detriment of consumers, and any predatory behaviour. These mechanisms shall take account of the provisions of the Treaty, and in particular Article 86 thereof³³”

There was no mentioning of how this regulation was to take place and no specific requirement for an independent regulator. There was also no mentioning of access conditions or regulatory independence. The role of the Commission was also limited, because all aspects of access were limited to national dispute resolution mechanisms which were not specified (Stern 1998: 98-100). As in the case for electricity, the Commission conceded to national positions and the industry. But yet again liberalisation measures were introduced, enlarging the area affected by the Internal Market. That way the Commission had a starting point for further liberalising the sector.

In 2003 the second step of liberalisation in the energy sector was completed. Two Directives were issued in combination to further liberalise the gas and electricity sector.³⁴ The provisions included the following steps to be implemented by 2007: unbundling of transmission system operators and distribution system operators from the rest of the industry, free entry to generation, monitoring of supply competition, full market opening, promotion of renewable sources, strengthening the role of the regulator and to have a single European market (Martin et al 2007: 322). These objectives mandated Germany to finally create a national regulator of the energy market, something they have refused to do for a long time. Still, the legislation turned out to be insufficient for the Commission to complete liberalisation. In addition to slow implementation of the legislation in member states, the energy companies were increasingly merging to avoid the policy (Martin et al 2007: 323). It was unclear whether the Commission and the regulators had enough power to actually force these

³³ Stern (1997: 98)

³⁴ Directive 2003/54/ EC concerning common rules for the Internal Market in electricity. Directive 2003/55/EC concerning common rules for the Internal Market in natural gas.

companies to break up. The Directive suggested that the Commission had the obligation to “report on aspect of market dominance”. The national regulators had more powers “to review changing ownership patterns” (Thomas 2005: 15-18). The result of this vagueness was increasing integration of energy companies with potentially devastating effects on competition (ibid):

“The pattern is clear- Europe’s larger electricity companies have been growing larger, acquiring footholds in new markets. These footholds could be used to compete aggressively across Europe, but the relatively limited number of really large companies, and the theory of multi-market contact, suggest a worrying alternative, that the European electricity industry would be become dominated by a few firms with little incentive to compete” (Green 2006: 2540 in Martin et al: 323)

This assessment may apply to both the electricity and gas sectors, because the large companies operate in both areas. One tool that the Commission can use to remedy the situation is to apply competition policy and threaten with infringement procedures against large companies. Another approach would be to propose new legislation to force member states to deal with their companies under EU law. The Commission chose both.

The next step of the Commission was the 2007 Sector Inquiry done by DG Competition. It revealed that the Internal Market was far from satisfactory liberalised.³⁵ Among the main findings of this inquiry were that European energy markets remain national in scope, concentrated and not sufficiently transparent. This, along with recommendations made by the European Council, led to the legislative proposals in the Energy Package. The most controversial aspects of these proposals are the full separation of ownership of transmission assets from the supply and distributions assets, and the introduction of an Agency for Cooperation of Energy Regulators. The package was launched in September 2007, and is to be decided upon during 2008. Whether this will happen is highly uncertain, given the special nature of

³⁵ DG Competition Report on Energy Sector Inquiry, 10 January 2007. SEC (2006) 1724

energy to promote national security. The notion of unbundling large energy companies brings fear that the strong companies will lose negotiating power towards external suppliers (Written reply to author). There is also widespread scepticism towards the notion of the Commission setting up an Agency that might look increasingly like a European Regulator, dependent on Brussels, infringing upon member state control over energy markets (Interview 6). To avoid the unbundling procedures Germany, France and six other member states proposed a “Third Option” to ensure sufficient TPA without selling transmission assets.³⁶ This proposal is at the moment discussed in the Council and Parliament. The Energy Package will be discussed in more detail later in the thesis and the next section reviews some of the external threats to EU energy supplies.

3.5 The external threat

The EU is highly dependent on gas imports to meet energy demands. Today the EU imports 54 % of gas consumption, a figure that is bound to increase (Kjärstad, Johnsson 2007: 873-4). Since more than 50 % of these imports come from Russia (Ibid), the EU can not neglect political considerations on energy policy when dealing with this major supplier.³⁷ This is why the EU has gradually increased its ambitions as an energy power, by trying to create an external dimension to EU energy policy. This policy is based on the three guiding principles of EU energy policy: competitiveness, security of supply and sustainable development.³⁸ Concrete measures introduced by the EU have included to expand the legislative scope of the Nice treaty, in the yet to be ratified Lisbon Treaty presented in 2007. The Nice Treaty is not directly concerned

³⁶ The link for the complete “Third Option” proposal is provided by Euractiv (29.1.2008): <http://www.euractiv.com/en/energy/france-germany-table-third-option-energy-liberalisation/article-169919>

³⁷ Major gas suppliers are: Russia 50%, Algeria 23 % and Norway 22 % of total gas imports to EU 25 (Larsson 2007).

³⁸ Commission (2006): Green Paper: A European Strategy for a sustainable, competitive and secure energy.

with energy security, even though some energy provisions in general are mentioned.³⁹ Energy is finally explicitly acknowledged as a part of the Internal Market in the Lisbon Treaty.

There are many concerns to take into account when creating a common external front in the energy sector. In 2007 the EU made several efforts to address the issue of energy security. It started with a Communication from the Commission in January 2007, and was followed up by Spring Council Recommendations in March the same year, calling for further coordination to deal with security of supply.⁴⁰ After this, security of supply measures was introduced in the Lisbon Treaty. This Treaty explicitly mentions solidarity between member states in case of an energy supply failure. In Article 100, it is proposed to include a provision in which the Council can adopt solidarity measures if facing supply failure. Furthermore, the proposal introduces a new article 176A which focuses on energy. Here, ensuring security of supplies is mentioned explicitly, but the competencies of the EU to act are rather limited.⁴¹

Even though formal competencies of the EU to act in the external energy dimension remains rather limited, there is no doubt about the seriousness of the effort of the EU to make a coherent energy policy. Dependence on Russia and other even more unstable regions, has led the Commission to address the issue of a coherent strategy to create a common external energy policy.⁴² The security of supply dimension of EU policy is closely related to previous liberalisation legislation. According to the European Commission, unbundling and thus more competition in all parts of the

³⁹ For example article 175, saying that the Council can adopt measures to change the energy mix of a country in the area of the environment (Hagihigi 2007).

⁴⁰ Commission of the European Communities (2007): Communication from the commission to the European Council and the European Parliament- An energy policy for Europe. COM(2007)1 and Council of the European Union, Brussels European Council 8/9 March 2007. Presidency Conclusions (7224/1/07)

⁴¹ Treaty of Lisbon (200)

⁴² Communication from the Commission (2006): External energy relations: from principles to action.

energy sector is the best way to secure energy supplies to Europe.⁴³ The Commission states that a strong customer base, not strong companies, is the key to secure energy markets.⁴⁴ Part of the reasoning is that producers want to supply a market with strong, good and reliant customers (Interview 5). In addition, if energy companies push the price of gas too high, customers might look for other energy sources. As China is emerging as a competitor to Europe for Russian supplies, these threats must be taken seriously (Spanjer 2006: 2896-7). Partly as a response to this the EU wants to disintegrate companies that control both the transportation and distribution of natural gas, so called vertically integrated companies. The EU argues that these companies are in fact threats to security, opposite of what the industry claim (Written reply to author). The industry states that strong companies are the basic condition for good bargaining powers toward the powerful production companies (written reply to author). On the other side, the EU stress that only competition will secure necessary investments in the Europe wide gas grid and ensure that all customers get access to energy, also in the case of emergency.⁴⁵

Even if the EU is able to dissolve vertically integrated companies, it will not solve the problem of the producer. The EU has a few producing countries, but as long as most of natural gas consumption is supplied from external sources, the liberalisation efforts of the EU in the external dimension can not easily be extended to production (Finon et al 2008: 424-427). Some of the vertically integrated companies own shares in production assets,⁴⁶ and the EU wish to achieve further upstream liberalisation.⁴⁷ This is difficult dilemma for the EU. Gazprom is the exclusive exporting company of Russian gas, and there are not sufficient incentives for Russia to liberalise this

⁴³ Communication from the Commission (2007): An energy policy for Europe.

⁴⁴ Communication from the Commission (2006): A European Strategy for sustainable, competitive and secure energy.

⁴⁵ Ibid.

⁴⁶ E.ON Ruhrgas owns 7 % of Gazprom (Larsson 2007).

⁴⁷ "Upstream" refers to the production and export of energy.

arrangement (Grigoryev: 2007). The EU is dealing with a non- liberalised trading partner with market concentration. As long as the Russian market is governmentally controlled, the EU must expect that energy can be used as a political tool (Röller et al 2007: 22). Furthermore, Russia has not ratified the European Energy Charter Treaty, which would oblige the country to open their market to a greater extent than at present (Geden et al 2006: 427-8). As long as the EU liberalises its own markets, without a similar opening of supplier markets, there is a great risk that monopolistic companies, like Gazprom, will integrate vertically into European markets. The extreme consequence of this could be that external actor control the whole chain from production to distribution without big competitors, because the EU will have abolished them (Larsson 2007: 26-29). The EU has perceived this risk, and proposes the controversial “Gazprom clause” in the Energy Package. This suggests that foreign companies that want to buy assets in the EU energy sector will have to prove their intentions for doing so to ensure reciprocity in liberalisation measures.⁴⁸ Full liberalisation can not fully replace security considerations, and political supervision and diplomacy is still of essence to secure good energy relations with external suppliers (Luiciani 2004: 4-7)

As long as external energy relations remain a national competency, in line with other CFSP measures, it is hard to imagine that member states will regard security of supply to the EU as more important than national priorities (Geden et al 2006: 9-13). This inherent problem makes the EU less credible as a coherent force in world energy politics. The outspoken EU effort to work for more competitive international markets is more of a unique stance in the world than a common move. Russia is by far a monopolistic gas producer, OPEC is run by a cartel, and other suppliers, such as Venezuela have their own national agendas. Even though there have been liberalisation efforts in other parts of the world, most notably the US internal market, this is far from common in the world of energy politics (Larsson 2007: 48-52). The

⁴⁸ Euractiv (18.4.2008): “Commission stands by “Gazprom clause”.

centrality of energy to the functioning of a country dictates caution and coherent approaches to supply. Part of this approach is long term arrangements with suppliers, something that often involves careful political considerations (Geden et al 2006: 11). This is not fully coherent with the goal of increased competition in the energy field, and shows the contradiction of EU policy. The friction between national strategies and EU policies is at the heart of the heated debate over an Energy Policy for Europe.

3.6 Climate change

The above considerations have failed to take into account climate change policy, which is of great importance in EPE. The Commission has the right of initiative in environmental policy and has used it to propose a climate package in January 2008. This is an ambitious package which seeks to strengthen the Emission Trading Scheme (ETS), by setting stricter limits for emission in richer countries. It is also setting standards for “clean” energy sources and energy efficiency.⁴⁹ The Commission has widespread support for acting on behalf of the European countries in this matter, even though the specific emissions quotas may be difficult to negotiate on (Interview 6). The Commission is systematically linking climate change and the Internal Market, which it has competencies in with security of supplies. This way, it might be difficult where to draw the line between divisions of powers, as the density of linkage between these policy areas increases (Haghighi 2007: 183).

In March 2008, right before the Spring European Council where the Heads of State meet, the Commission and the High Representative of the Council together with the issued a report linking climate change with energy security.⁵⁰⁵¹ This means that in

⁴⁹ The policy is explained in Commission (2008): “20 20 by 2020 Europe's climate change opportunity”.

⁵⁰ High Representative and the Commission (2008): Climate change and international security. http://www.consilium.europa.eu/ueDocs/cms_Data/docs/pressData/en/reports/99387.pdf

⁵¹ The High Representative coordinates the Common Foreign and Security Policy (CFSP) of the EU. It is based in the Council General Secretariat and is currently headed by Javier Solana. Lewis (2007: 166-7).

addition to treating the Climate and Energy Package legislative proposals, the European Council was offered this link as well. The Energy Policy for Europe is now recognised as a policy area for the EU, and it seems unlikely that the Commission will retreat from being the agenda setter in this respect. Still, the ongoing debate between member states and the Commission over the content of this policy shows the controversy always present in energy policy. The analytic part of this thesis will offer empirical and theoretical contributions to how the energy power game unfolds.

4. Case one: The energy power game

4.1 Competition Policy

When looking at the history of European gas policy, it is particularly striking to see how the Commission has pushed for almost unthinkable legislation, without having explicit legal competencies in the EU Treaties to do so, and with strong resistance from the member states (Stern 1992: 55-80). To understand this, there are a few notes to be made about the way the Commission uses existing legal competencies into new policy areas. For instance, the Commission has been successful in using the competencies in the competition policy area (Matlary 1998: 106-24). By using the competition provisions in the EU Treaty, the Commission has the power to intervene in the market of member states if they infringe upon the Internal Market:⁵²

Art. 81: “The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market”

Art 82: Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market in so far as it may affect trade between Member States.

⁵² The Consolidated version of the Treaty establishing the European Community. Official Journal of the European Communities: C 325/33

Art 85: 1. Without prejudice to Article 84, the Commission shall ensure the application of the principles laid down in Articles 81 and 82. On application by a Member State or on its own initiative, and in cooperation with the competent authorities in the Member States, which shall give it their assistance, the Commission shall investigate cases of suspected infringement of these principles. If it finds that there has been an infringement, it shall propose appropriate measures to bring it to an end.

2. If the infringement is not brought to an end, the Commission shall record such infringement of the principles in a reasoned decision. The Commission may publish its decision and authorise Member States to take the measures, the conditions and details of which it shall determine, needed to remedy the situation.”

These are strong powers of the Commission, but there is certainly no mentioning of energy in this. The Commission did get help from the European Court of Justice (ECJ) to confirm the position of competition policy in the energy sector. The Almelo ruling⁵³ of 1994 stated that electricity is like any other good and thus not necessarily a public service (Matlary 1998: 122). This has important implications also for the gas sector, because it relates to the nature of energy as a public service. This landmark ruling specified that companies must demonstrate why they would need market restrictions, so that the burden of proof was turned to the companies rather than the Commission. As the Commission holds great powers in the competition segment, this ruling confirmed that application of these provisions was in fact sanctioned by Community legislation. The threat of infringement procedures is a strong tool for the Commission, and has been used frequently during all liberalisation efforts in the energy sector (Matlary 1998: 119- 124). One of the reasons why this would be a strong threat is that member states are assumingly afraid of ECJ activism. If the Commission succeeds in litigating against strong national companies, it could set a precedent for the whole sector which would look bad for the profile of companies and the nations they operate in. The role of ECJ in promoting integration should thus not be underestimated (Schmitter 2005: 267).

⁵³ Almelo v. Isselmij, C393/92

The agenda setting power of the Commission should not be neglected in this respect. Calling for such radical measures in the wake of the European momentum in the late 1980s needed to be taken seriously (Matlary 1998: 22-23). There were high political expectations about Community action in all parts of the economic sector, and financial elites in Europe had started to forge close ties with the Community institutions (Fligstein et al: 81-85). As soon as this proposal was issued, the member states and energy companies started to listen to the Commission in the energy sector (Interview 3,5). This would suggest that as soon as the background conditions for integration were present, the Commission was able to push spillover into the energy sector. It must be stated here that there is no evidence of automatic spillover. The energy sector was not explicitly mentioned in the Single European Act, and the nationalised energy markets were thoroughly established after three decades of national interests (Stern 1998: 10-33). This suggests that the spillover of the Internal Market into energy was the result of Commission activism and could rather be labelled political spillover under favourable external conditions (Jensen 2007: 90-91) (Rosamond 2000-72).

Another aspect of energy integration that should be discussed is the legal basis of EU action. As mentioned above there was no explicit mentioning of energy in the EC Treaty. Still, the Commission was able to put energy on the agenda using the telecommunications sector as a door opener (Matlary 1998:120). This issue linkage policy started with introducing competition policy as a legal basis for Community action in the energy sector. This strategy was a bold, but also very successful move. By using the competition arrangement in the telecommunication sector, the Commission set precedent in a less controversial policy area (Ibid). Under the competition procedure, the Commission can take legal action against companies and regulate the market, giving it a strong role in energy policy development (Stern 1993 57-69). With the help from a favourable ruling from the ECJ the Commission could use issue linkage between the telecommunication sector and the energy sector to forge the gas and electricity transit directives (Matlary 1998: 120).

The process of European energy integration has been very interesting in that it captures inherent tensions in European integration. It is remarkable how the Commission again and again has put energy on the agenda. It has been defeated several times in the Council regarding the use of legislative clauses and concessions such as the “single buyer” proposal of France in the electricity sector (Stern 1998: 90-95). Still, as these concessions have been made there have always been developments towards liberalisation. Starting with transport and telecommunications, the Commission has increasingly expanded the scope of the Internal Market from “soft policy” areas to areas with implications for the welfare of the nation state. This has been done in a fashion that I would coin as the “propose and concede” method, proposing radical measures and conceding on parts of it in a repetitive manner, gaining a bit more competencies in each step. The Commission repeatedly “loses” fights with member states over certain proposals, and they must know that these proposals are difficult to implement.⁵⁴ An interesting example is the case of the Common Rules Directive negotiations in the early 1990’s, where the Commission issued a Consultative Committee (Stern: 1992 74-76). In this committee only the Commission supported its own proposals, but now the whole industry is turning towards liberalisation, voluntarily or not. In fact, the inclusion of the industry in the decision making process provides the Commission with a new avenue of influence, because it creates political expectations and force the industry to deal with the Community level (Matlary 1998: 113).

Another interesting aspect is how the Commission has been able to use its own activism to give itself a legal basis for decisions. This was the case in the 1990s, when the Commission got a formal role in monitoring the gas grids through the Trans-European networks, after having given this role to itself (Matlary 1998: 109). This was also the case with the Energy Charter Treaty which the member states initially failed to agree upon. The Commission seized the moment, and met informally with

⁵⁴ The Commission always have extensive consultation with all interest groups prior to legislative proposals. El-Agraa (2007: 47)

the Russian negotiators. By the time member states had got their positions straight the Commission had already mapped the policy area and drafted proposals. This way the Commission defined itself as the leading actor in the Charter Treaty process, taking a role with implications beyond the Internal Market (Matlary 1998: 138-9). It could be argued that this role of the Commission as an agenda setter, and thus in effect agent of guided spillover, has been further strengthened with the Lisbon Treaty. In the next section it will be shown how energy provisions are finally recognised as Community competencies.

4.2 The Lisbon Treaty

Before analysing the Energy Package, it is worth spending some time on the Lisbon Treaty. This Treaty is not yet ratified by all member states, and it might also undergo the scrutiny of referendums in some countries. Even though the Treaty is not yet an applicable legal document, it is remarkable to see how well the efforts of the Commission in the energy sector have fared. Now there is finally a legal basis for Community action in the internal and external dimension of energy policy:⁵⁵

The proposed Article 176A reads:

“1. In the context of the establishment and functioning of the Internal Market and with regard for the need to preserve and improve the environment, Union policy on energy shall aim, in a spirit of solidarity between Member States, to:

(a) ensure the functioning of the energy market;

(b) ensure security of energy supply in the Union; and

(c) promote energy efficiency and energy saving and the development of new and renewable forms of energy; and

(d) promote the interconnection of energy networks”.

⁵⁵ Treaty of Lisbon (2007)

However, in the next section it says:

“2. Such measures shall not affect a Member State's right to determine the conditions for exploiting its energy resources, its choice between different energy sources and the general structure of its energy supply, without prejudice to Article 175(2)(c).”

Also interesting is the proposed Art. 100, Paragraph 1, which says:

“ Without prejudice to any other procedures provided for in the Treaties, the Council, on a proposal from the Commission, may decide, in a spirit of solidarity between Member States, upon the measures appropriate to the economic situation, in particular if severe difficulties arise in the supply of certain products, notably in the area of energy.”

These provisions give extensive power to Community institutions for action in the energy sector. After many years of “proposals and concessions” the member states have now agreed that energy is part of the Internal Market. This is of course nothing new, but the legislative basis makes the Commission, as guardian of the Treaties, obliged to make sure that liberalisation of the sector is completed (El-Agraa 2007: 43). However, it is interesting to see the tension between section one and two in Article 176, in which member states are very reluctant to give the EU the right to specify energy mixes. Increasingly, the Commission is getting assertive into this area as well (Interview 4). This is strengthened by Art. 100 that give the Commission an agenda setting role in the security of supply considerations. Before turning to this aspect of the Energy Package, the next section will provide an empirical example of member state resistance to EU liberalisation. This serves to show how the Commission uses its strengthened energy position in an even more assertive way than before.

4.3 The energy package

In September 2007 and January 2008 the Commission issued two legislative packages dealing with energy and the environment. The Energy Package seeks to complete the liberalisation of the Internal Market in energy and establish a European Regulatory Authority.⁵⁶ The legislative package on renewable energy and climate change was issued 23 January 2008 and seeks to enhance production of renewable energy and limit CO₂ emission.⁵⁷ In this section I will focus on the legislation concerning natural gas and the establishment of a regulatory authority. In the next part of the thesis I will show how these legislative packages are treated in combination, in a strategic attempt to use issue linkage between energy and climate change. The last chapter will compare these to cases.

The Energy Package contains several controversial proposals. The most delicate issues concern the dissolving of vertically integrated energy companies and the establishing of an agency to combine the efforts of national energy regulators (Interview 6). The Commission states that the current level of ownership unbundling between supply, transmission and distribution of gas is not sufficient to create incentives for competition in the pipelines. Prior to the Energy Package the Commission conducted a sector inquiry, stating that:

⁵⁶ The proposals include: Amending Directive 2003/54/EC concerning common rules for the Internal Market in electricity, amending Directive 2003/55/EC concerning common rules for the Internal Market in natural gas, Regulation establishing an Agency for the cooperation of Energy Regulators, amending Regulation (EC) No 1228/ 2003 (on cross-border trade in electricity), amending Regulation (EC) No 1775/ 2005 (on access to gas transmission systems).

⁵⁷ For more about the environment and climate change package see the Commission webpage http://ec.europa.eu/environment/climat/climate_action.htm

*“ The shortcomings identified in these key areas calls for urgent action and priority should be given to four areas: (1) Achieving effective unbundling of network and supply activities, (2) removing regulatory gaps (In particular for cross-border issues), (3) addressing market concentration and barriers to entry, and (4) increasing transparency in market operations.”*⁵⁸

According to the Commission, These provisions are necessary to remedy persistently high wholesale prices, barriers to entry and limited customer choice in the whole sector.⁵⁹ Legislation so far has created a multi-faceted pattern of ownership in Europe. Some countries have completely separated transmission companies, while others have created legal entities within the companies controlling the transmission.⁶⁰ The latter approach is deemed inadequate by the Commission. In the Energy Package the Commission proposes two concrete options for unbundling the vertically integrated companies: The first option is full ownership unbundling, meaning that the vertically integrated companies must sell the part of the company dealing with transmission. This is the preferred option of the Commission. The alternative option is to have an independent system operator (ISO) which will ensure that transmission networks are treated outside the influence of the vertically integrated company. The company can retain the ownership assets, but the network itself must be operated by a completely separate entity. In addition to the aforementioned concerns, the key advantages to an independent operator are to ease the access of competitors to the networks, provide more comprehensive and unbiased information about network capacity and to prevent distorted incentives for investments. The latter may occur when companies wish to protect their home market, and thus avoid investing in competing infrastructure⁶¹.

⁵⁸ 10.1.2007, COM (2006) 851 final. Inquiry pursuant to Article 17 of Regulation (EC) No 1/2003 into the European gas and electricity sectors (Final Report)

⁵⁹ Commission (2007): Explanatory Memorandum of the 3rd Energy Package.

⁶⁰ Ibid.

⁶¹ Commission (2007): Explanatory Memorandum of the 3rd Energy Package.

The second controversial issue relates to the establishment of an agency for the cooperation of national regulators. In the gas directive of 2003,⁶² all member states were required to set up a national regulator, and this was done as late as 2005 in Germany. With this new proposal the role of this regulator is strengthened to ensure that *“the regulatory authority has legal personality, budgetary autonomy and adequate human and financial resources to carry out its tasks”*.⁶³ In addition, the Commission wants to strengthen the cooperation between national regulators to ensure better conditions for cross- border competition. This could be done by creating an independent regulatory body with necessary authority to monitor EU- wide regulation. Concretely the Commission proposes to establish an agency which will be given the task to coordinate market “codes”, research and development, grid operation and investment planning.⁶⁴ As always before when the Commission have made radical proposals for the energy market, the industry and central member states fiercely oppose such efforts. Germany has taken the lead in this process.

4.4 The German gas market

The German market has some structural features that are challenged by the Energy Package. The market is characterised by large dependency on imports and long term contracts with foreign suppliers, most notably Gazprom (Sander 2006). The internal organization of the market is basically divided among four large companies, a result of several mergers starting in the late 1990s⁶⁵ (Brunekreeft et al 2004: 2-11). In the post- war era, transmission companies controlled the market by “concession and

⁶² Directive 2003/55/EC concerning common rules for the Internal Market in natural gas. Official Journal of the European Union: L/176/57

⁶³ “Proposal for a Directive amending Directive 2003/55/EC concerning common rules for the common market in natural gas.” 2007/0196 (COD)

⁶⁴ Commission (2007): Explanatory Memorandum of the 3rd Energy Package.

⁶⁵ The companies are RWE, E.On Ruhrgas, EnBW and Vattenfall. These companies controlled 90, 65 % of the German energy distribution in 2003 (Brunekreeft et al: 2006).

demarcation” agreements. This involved two steps; firstly, the transmission companies split the market between them. Then, the most often publicly owned distribution companies signed concession agreements stating that they would not chose other suppliers than the one in their area (Stern 1998 139-151). This way, the supplier could secure high prices, something that the both the federal and local level of government supported.⁶⁶ This led to a double payment for the customers, first to the company and then to the local government. EU driven liberalisation in the gas sector had an impact on Germany in the late 1990s. This way the “concession and demarcation” arrangements were dissolved (Ibid). The response of the industry was to merge. This was especially the case with transmission companies, and they started buying distribution companies after merging between themselves (Brunekreeft et al: 2004:2-11). Today Germany still has very high prices for energy, and only 5 % of consumers are able to change suppliers freely (OECD: 2006).

The German organisation of the market is highly controversial, and the EU has imposed several measures to liberalise it. These include the introduction of a national regulator in 2005, and legislation for third party access (TPA). Still, the German government regards large companies as important to make its own market less fragile and stronger in the competitive international markets (Sander 2006). The German Ministry accepted the merger of E.ON and Ruhrgas in 2002, making it one of Europe’s largest energy companies (Zenke et al: 2003). The result of this merger of was that the gas transportation and distribution system was vertically integrated, since Ruhrgas controls 50 % of wholesale supply and 1/3 of transmission pipelines for natural gas in Germany (OECD 2006). This was at best questionable under German and EU competition law and was struck down by the Federal Cartel Office and The Monopolies Commission in Germany. These institutions argued that in addition to the clear violation of competition law, there was nothing that indicated that Ruhrgas

⁶⁶ As noted earlier, the federal government wanted to limit the amount of gas used in electricity generation for strategic reasons. Local governments most often owned the distribution companies, used excessive gas prices to cross- subsidise other public services (Stern 1998: 12).

would be unable to compete with other gas companies for supplies if it were not merged with E.ON. Furthermore, they argued that security of supplies would be better taken care off in a competitive system, avoiding bottlenecks through only one company,⁶⁷ E.ON appealed to the German Ministry of Economics, who can override the Federal Cartel Office on the grounds that “the restraints to competition are outweighed by advantages to the economy at whole”. This was indeed the Ministry’s opinion. 5 July 2002 state secretary Dr. Tacke issued authorisation to the merger of E.ON and Ruhrgas. Minister Muller, who was previously employed by one of the companies that later became E.ON, justified the arrangement on the grounds that it was necessary to merge the companies to improve security of gas supply to Germany (Zenke et al: 2003). The company later bought 6,5 % of the stocks in Gazprom, and is now one of the owners of the Nord Stream pipeline, that is currently under construction directly connecting Germany to Russian gas markets (Sander: 2006).

This unique structure of German market organisation, with four large privately owned companies and the dependency of Russian gas imports make the Energy Package a sensible issue for the German government. Currently, the country is taking the lead with seven other member states to go ahead with an alternative solution for the vertically integrated companies.⁶⁸ The “Third option” is in essence a status quo position, protecting the large energy companies (Interview 4). In the proposal, member states should be able to choose between full ownership unbundling, ISO and the provisions proposed by the eight countries.⁶⁹ The main feature of the latter option is that vertically integrated companies can maintain ownership of the transmission network, given that the daily operation of the network is kept independently from the rest of the company. Concretely, this means that the board of directors of the

⁶⁷ This is almost identical to the reasoning of EU institutions for security of supply aspects of market liberalisation.

⁶⁸ Draft: Effective and Efficient Unbundling of Transmission System Operators (“Third Option”). The proposal can be viewed on: http://www.euractiv.com/29/images/Franco-German%20draft%20lib%20proposal%20080129_tcm29-169922.doc

⁶⁹ The eight countries are: Austria, Bulgaria, France, Germany, Greece, Luxembourg, Latvia and the Slovak Republic.

transmission company have a minimum number of years quarantine before being able to work in the mother company. The ownership will be a joint stock venture, securing ownership of the parent company. The transmission company will make independent operating decisions, but the investment decisions need to be approved annually by the parent company.⁷⁰

This proposal might look similar to the second option of the Commission, the ISO proposal. However, there is one great difference; the ISO solution would be completely independent, with no regulatory insight from the owner company. In the “Third option”, financial planning and access to the grid would be under the control of the parent company. So even though the parent company does not interfere with the day to day operation of transmission and third party access, the operation must be within an approved financial framework, making the parent company highly influential⁷¹. The proposal was published on 29 February 2008 in the Spring Energy Council, but the same day E.ON Ruhrgas made a very surprising announcement.

The company announced to sell the grid on the same day that the German government presented the “Third option” in the Spring Energy Council in Brussels. This move caught most people by surprise, and many journalists and decision makers immediately thought that this would make the “Third option” completely obsolete.⁷² The German government was informed about the decision, but it did not know about the timing (Interview 5). This makes it easy to jump to the conclusion that the Commission staged the whole announcement, with the news dropping *during* the negotiations. This is something that is difficult to verify, and obviously EON as a private company can make these kinds of decisions whenever they feel the need. However, it is a fact that the Commission is conducting infringement procedures

⁷⁰ For a policy summary of the “third liberalisation package” see Euractiv link dossier (first published 4.10.2005): Liberalising the EU energy sector. <http://www.euractiv.com/en/energy/liberalising-eu-energy-sector/article-145320>

⁷¹ For a brief overview of these implications see: <http://www.euractiv.com/en/energy/france-germany-table-third-option-energy-liberalisation/article-169919>

⁷² European Council Press Conference 28.2.2008: <http://ceuweb.belbone.be/search.php>

against EON and other large European energy companies for market abuse (Interview 2, 3). It could therefore be claimed that EON conceded to sell the electricity grid to get a break from the ongoing investigation (Interview 2). It must be noted here that EON said nothing about selling the gas grid, something that is far less sensitive for the energy companies (Interview 3). EON has later proposed that the government should buy the grid, a move that would avoid other companies controlling it. It is highly unlikely that the German government would do that (Interview 5), but it is an interesting prospect because it would actually work against deregulation of the energy sector (Interview 9).

4.5 The Commission and the member states

The Energy Package, the “Third Option” and the surprise announcement of E.ON Ruhrgas is all part of a political game in Brussels over the pace of integration. There are many angles to look at this. First this could be regarded as an “intergovernmentalist” quarrel. In this we could see the German resistance as a proof that member states are still in charge, and that national interests prevail in EU decision making. Another angle is to look at this as a proof that the Commission is setting the agenda and pace of integration in the energy sector, and thus have a few “tricks” up its sleeve to make integration run more smoothly. The next section will analyse these notions.

In the energy policy sector, Germany has always been opposed to radical measures (Stern 1998: 139-151). The special nature of policy areas in the different member states calls for a national position in Brussels. With the Energy Package there is a feeling among German stakeholders that the legislation is targeted directly at them (Interview 3). When it comes to liberalisation in the gas sector, Germany has always been reluctant (Stern 1998: 139-151). It opposed the gas transit directive, and had serious concerns about TPA arrangements. These efforts can largely be attributed to the protection of the privately owned gas companies, because in the pre- SEA era,

these companies and the government operated with a tacit agreement to secure stability of gas supply (Stern 1998: 10-32). Thus, there are several arguments that would support the notion of national priorities guiding the German approach to EU decision making.

4.6 German opposition 1: The external dimension?

Firstly, there is the aspect of security of supplies. Germany is heavily dependent on imports from Russia. Around 70 % of German energy use comes from gas and oil, and Russia has the largest import share (Sander: 2006). These deliveries are mostly made with long term contracts, and two companies have negotiated most of these, Ruhrgas and Wingas.⁷³ Wingas is a subsidiary of the chemical giant BASF, and they have formed a joint venture together with Gazprom as an alternative to Ruhrgas. These pipelines run in competition with Rurgas, as traditionally Ruhrgas has covered imports of Norwegian gas to the whole continent, while Wingas has dealt with imports of Russian gas (Stern 1998 139-142). This is about to be modified as Wingas, Ruhrgas and Gazprom now operates together in the Nord Stream pipeline project in the Baltic Sea. With these new arrangements the imports of natural gas is even less competitive as Ruhrgas and Wingas completely dominate Gazprom relations (Brunekreeft et al 2004: 8-11). This could explain why these companies are afraid to jeopardise agreements with Gazprom by losing control over the transmission network. This is indeed a very large concern for the gas industry, which oppose the unbundling of the gas network for security reasons:

⁷³ Wingas is a subsidiary of both Wintershall and Gazprom. Wintershall is owned by BASF.

(...) (Proposals) are undermining or hindering activities abroad (concepts of ownership and ISO unbundling, regulation of European competitive energy commodity markets). Several proposals will create risks regarding operations outside the EU (especially for gas within the relation to the suppliers/producers). (...) Big natural gas projects for Europe require strong partners on both sides, the exporting countries and the importing countries. In the EU gas sector the proposed unbundling rules are not in favour of supporting the importing companies position and they will not support the development of new gas infrastructures (Written reply to author: 2008)

The security of supply aspects may be important to the German government and the industry, but it is not the most prominently argued reason for resistance. According to Sander (2006), the “special relationship” between Russia and Germany in the gas sector is mainly a relationship between companies. However, other people argue that there was a political backdrop to the negotiations over the Baltic Sea pipeline. Gerhard Schröder is now in the Board of Directors in the pipeline project and personal relations can help to secure a good business climate for European gas imports (Interview 2). It must also be noted that security of energy supplies has not been a political priority in Germany until the Ukrainian gas crisis in 2006⁷⁴ (Umbach: 2006). This make it is hard to argue that the position of German energy companies towards Gazprom is the only reason for German resistance to unbundling, even if it seems to be an implicit concern. Another aspect undermining this argument is that EON actually wants to sell off its electricity grid. A representative of the German gas industry put it this way:

“(...) Officially we say that this (to sell the transmission company) could be damaging security of supply. On the other hand, if you now see that one big company is doing it, you could question if this argument could be put on the table. (...) So far the argument that the unbundling could cause problems for security of supplies is a stronger argument on the gas than electricity grid. That could be the reason why EON is not announcing to sell their gas grid” (Interview 3)

⁷⁴ Russia cut off gas supply to Ukraine in January 2006 after an apparent price dispute. Ukraine is the main transit country for gas imports to Europe, so this crisis proved the vulnerability of European gas supply. For more about the Ukrainian gas crisis see: Stern (2006): “The Russian- Ukrainian gas crisis of January 2006”

4.7 German opposition 2: internal considerations?

The dominant position of these companies can readily explain the past twenty year efforts of resistance. Still, both the Commission and the German government argue through a market perspective. Officially the German government deny that security of supply is part of the reason for not accepting the unbundling provisions (Interview 5). In stead they argue that selling the transmission network would be an unfair intervention on private companies (Ibid). One representative of the German industry compared ownership unbundling to “*force a car manufacturer to sell its factory*” (Interview 3). They would claim that there are no guarantees that having an independently owned transmission network will increase TPA and competition, given the special nature of gas supplies and long term contracts. Thus, the view is that the industry can deal with TPA under the current provisions of legal unbundling.⁷⁵ Furthermore the industry argues that the introduction of a national regulator in 2005 was sufficient to remedy market imbalances (Interview: 3). However, the industry admits that introduction of a national regulator in Germany has only had a significant impact on the electricity sector (Interview 2)⁷⁶. Looking to other countries is yet another argument from the industry:

“ So our argument of access to the grid is not about who owns the grid, you got windmills in northern parts of UK that can not be connected to the grid, (...) it is a question of quality of regulation and how to secure that the privileged power plants get access to the grid” (Interview 2)

The last Internal Market consideration is that of network security and investment. Many people have difficulty in seeing who will invest in the grid when the operator is not going to use the same gas for supplies. This could be a valid argument if a company that does not own the gas do not want to upgrade the gas infrastructure.

⁷⁵ Meaning that the transmission company is its own legal entity, introduced by the last round of liberalisation in 2003.

⁷⁶ For a detailed study about the history and impact of the German regulator see: Brunekreeft et al (2004): *Regulation, Competition and Investment in the German Electricity Market: RegTP or REGTP?*

Paradoxically, parts of the German industry have realised that there are not necessarily any differences in who owns the grid in this respect, because both vertically integrated companies and mere grid operators must have a return on investment, secured by the regulator, to make it profitable (Interview 6). In fact, EON was supposedly partly acting out of economic reasons when selling their electricity grid, because the cost of operating it is apparently is not worth the benefit of maintaining it (Ibid).

Certainly, EON would not sell their grids as easily without infringement procedures against them, but it was known for a long time that they thought about selling it anyway (Interview 6). EON now wants the government to buy the grid something that might be a bigger fear for the government simply because it would be very costly (ibid). In the light of the aforementioned concerns over the German energy market it might be best to let the German government sum up its market concerns for unbundling:

“ We think that ownership unbundling in the strict way proposed by the Commission is not the most effective way, nor the most sure for investment coming into the network that we desperately need, nor the best way to bring down prices, because if you look at prices in countries that have this unbundling, there is no pattern that shows you that prices are lower. So we don’t think the Commission has a very strong case here” (Interview 5).

The Commission would respond that it in fact has a good case. To the first argument the Commission would say that investments in the infrastructure are actually lower because the incumbent companies are reluctant to invest in the infrastructure of the competitor. This way network investment in Germany and other parts of Europe is made dependent upon the business motives of a few companies. The Commission would argue that the regulators should have the independence and capacity to see that these infrastructure upgrades are made, ensuring security of supplies.⁷⁷ Concerning

⁷⁷ Commission (2007): Explanatory Memorandum of the 3rd Legislative Package on energy.

prices, a 2006 OECD report on the German energy market identifies an expensive market that is difficult to enter. Energy prices are consistently high. In addition, with E.ON Ruhrgas controlling 50 % of the wholesale market, and the trend that liberalisation has been followed by vertical integration makes it very difficult for new entrants to the market. The OECD report follows the same argumentation of the Commission and calls for stronger regulatory overview and the separation of transmission from supply and distribution (OECD: 2006). Certainly, nothing can be taken for granted about the consequences of unbundling. Especially the arguments about network security and viability of mere network operators need to be taken very seriously. Still, it is tempting to look at this as a protest against Commission intervention and consequently a status quo position.

4.8 German opposition 3: Enough is enough?

Even though the Commission will never admit that they are targeting legislation directly at one country, unbundling provision directly relates to the German market. As most other countries have nationally owned grid, this will not affect them as much:

“For countries that have state owned operations of course unbundling is easier to do if it means that you transfer running one part (the grid) in one ministry, and another part in another ministry. Is this really what they intended? (...) You have to ask yourself who ownership unbundling is actually targeting” (Interview 5)

This shows that Germany might be fighting for its national integrity; the whole issue of ownership unbundling becomes a question of “us versus them”. Interestingly, the “Third option” proposal is vigorously supported by France, even though the French grid is state owned (Interview 9). France is not severely affected by the Energy Package, but they might be afraid of rising EU competencies (interview 9). In an interview, the leader of the French network operator RTE stated that the opposition is

in part a response to a worrying ideological pro-liberalisation stance.⁷⁸ In Germany many stakeholders are concerned about the treatment of E.ON, which can be seen as a way for the Commission to blackmail countries with infringement procedures against private companies (Interview 9). The industry notes that this is a “backward” way of dealing with legislation, using proposed legislation to force a company to sell the grid before it is even treated in the Council and Parliament (Interview 2). Some would even claim that the Energy Package is driven by UK and the Netherlands to get access to German infrastructure when they run out of gas domestically (Interview 9). To this it must be noted that the UK has always been a frontrunner in the liberalisation of energy markets, where this process started earlier than in the EU (Stern 1998: 119-131).⁷⁹ These sentiments enhance the feeling that national stances remain important in the energy sector, something that is just as strong when it comes to the idea of a European regulator.

The fact that the Commission wants to establish an agency that will monitor and coordinate national regulators is met with scepticism. This move will make the Commission more in charge of national jurisdictions, critics claim. Up until 2003, regulation was not even considered necessary in Germany (Auer: 2003). Now, a few years after it was introduced all stakeholders that were interviewed for this purpose agrees that more coordination among national regulators is needed, but they are equally worried about the status of such an agency. One stakeholder from the German gas industry noted:

“(...) it is funny that they demand from the national regulators to be independent of the government, on the other hand they try to establish some sort of authority in Brussels, of course strictly dependent on the Commission” (interview 6)

⁷⁸ Euractiv: 6.3.2008. <http://www.euractiv.com/en/energy/interview-french-grid-chief-denounces-eu-ideology/article-170787>

⁷⁹ For more about the UK energy strategies see: “*Meeting the Energy Challenge. A White paper on Energy May 2007*”. Department of Industry and Trade. <http://www.berr.gov.uk/files/file39564.pdf>

There is a genuine concern that since the Commission already have the right of initiative it is important that there are clear boundaries to the competencies of the European regulator. Therefore, the Agency should only deal with cross-border issues and not interfere with national regulation (Interview 2). In stead of having an overarching regulator, the Commission should respect the competencies of the national regulators in stead of harmonising every single step. What should be harmonised are the competencies of each national regulator, not their operations as such (Interview 3). The industry is also far from content with the Commission rationale for the Energy Package. This relates to the sector inquiry done for the Commission impact assessment leading to the Energy Package proposal, regarding both unbundling and a European regulator (Interview 2). Firstly, the industry claim that the sector inquiry was conducted with old data, from the era before the national regulator was established in Germany. Secondly, when evaluating the national regulators, the data were not sufficiently objective:

“ (...) the Commission sent some kind of form to the national regulators and they describes the situation as they saw it in their country. For example, in Poland regulatory authorities would never say: we are not independent. (...) everyone knows that Poland has a very big problem with that. So this was biased, it was not made by the Commission itself” (interview 2)

The idea of the Commission as an adversary institution to the German gas industry is not new (Stern 1998: 139-151), and is certainly still an issue in the debacle over the Energy Package. Furthermore, the above discussion could strengthen the notion that national sentiments and policies are decisive for EU integration. The following section will review the position of the Commission in the light of member state resistance, placing the Energy Package in an historical perspective.

4.9 Commission persistence

The discussion about the Energy Package reveals a plethora of reasons for resistance from one of the most central member states. It is difficult to predict what the outcome will be, and when an agreement is made. With EU energy policy making in mind we should expect another concession from the Commission. Recently, at the time of writing, the Commission announced that it had in fact made an alternative unbundling proposal that would more easily satisfy Germany and France to make a deal in the June 2008 Energy Council.⁸⁰ The result remains to be seen, but the power game in Brussels is interesting even without an outcome. It is a snapshot of EU decision making that should not be taken out of its historical perspective (Rosamond 2005: 247). It is interesting to see how the Commission operates to push this legislation, and also how it is resisted. This game has been going on for twenty years with proposals and concessions in a process of integration. In the discussion below I will try to establish how this snapshot of EU integration serves to show how the Commission has been able to establish one very important thing; an ever emerging increase in political expectations of the Commission as an agenda setter.

When evaluating the role of the Commission in promoting energy liberalisation it is important to look at what has been accomplished. The sector is more liberalised than ever before, despite resistance. To illustrate this I would like to compare to statements from the German gas industry made in 1991 and 2008:

Gas industry response to the Gas Transit Directive (1991):

“The German gas industry is willing to adopt a constructive approach to the transit function. In this respect the European Community Transit Directive was superfluous. It has always been possible to come to commercial arrangement on all transit issues.” (Stern: 1993)

⁸⁰ Euractiv (16.5.2008): Compromise in sight on energy liberalisation. <http://www.euractiv.com/en/energy/compromise-sight-energy-liberalisation/article-172415>

Gas industry response to the Energy Package (2008):

“The best way to increase competition and to guarantee non discriminatory network access is not the expropriation of asset owners and the regulation of competitive energy markets, but the focussed pursuit of a truly Single European Market through the expansion of cross-border infrastructure and even further integration of the European energy markets. (Written reply to author: 2008)

This comparison is interesting in many ways. It says that the German industry is listening to EU legislation. Furthermore, the industry has changed from regarding European regulation as being superfluous in 1991, to being an advocate of European integration. This dramatic change in the view of EU integration can be seen as a proof that there have been a shift in loyalty to a new decision making level during the last seventeen years. This is further strengthened by the following position of a German gas company:

“The proposals are aiming to create a more efficient Single European Market. Companies which are ready to act as European companies may use opportunities to develop business activities.”(written reply to author: 2008)

On the other hand the industry is in 2008 persistently opposing regulation of the competitive markets. The idea of business being capable of dealing with market issues itself is prevalent. To this it must be noted that in a written reply from the gas industry to the author of this thesis, support the notion of a European regulator, as long as the boundary between national and European regulation is clear. The question of a European regulator is another interesting aspect of loyalty shift.

The industry now put all faith in the national regulator, which is an interesting turn in events, since Germany only after 2003 introduced one (Brunekreeft et al 2004). To recapitulate from the history of European regulation, it is interesting to see how the lack of a regulatory has been the most severe limit to the prospect of a European market (Stern: 1998: 98-100). Now there are clear rules of the operation of national regulators:

*“Member States shall designate one or more competent bodies with the function of regulatory authorities. These authorities shall be wholly independent of the interests of the gas industry. They shall, through the application of this Article, at least be responsible for ensuring non-discrimination, effective competition and the efficient functioning of the market, (...)”*⁸¹

Still, in the view of the Commission even this is now not sufficient to ensure competitive markets, and there is an apparent need to ensure that the national regulation is sufficient from a European perspective. This is a bold move from the 1998 settlement where the Commission failed to secure even national regulators (Stern 1998: 98- 102). It is remarkable to see how the Commission has achieved national (and even European) regulators and a legal base for TPA, and thus have reached the main goals of the “Internal Market” paper in 1988. Most importantly it has created a loyalty shift among stakeholders, in which the companies and national governments are very attentive to EU legislation in the energy market (Interview 2,3,5,6). This way, political expectations are in some respects even more centred at the EU level than the national level, especially in the case of new legislation concerning the Internal Market.

The role of the Commission in driving the integration process must not be exaggerated. There are a few constraints that must be duly noted. Certainly, when European gas markets are open for competition, there will be an enhanced need for cooperation, this is something that all stakeholders can agree on (Interview 3,5). The gradual opening up of the market with the “propose and concede” method of the Commission has created a gradual need for oversight. In this respect the role of major domestic markets should not be underestimated. The German gas market was already in the process of competition when TPA was initiated, with Wintershall building parallel pipelines to that of Ruhrgas (Stern 1998: 139-151). Even though common

⁸¹ Directive 2003/55/EC concerning common rules for the Internal Market in natural gas.

rules are necessary to create a level playing field, market developments are important to integrate companies (Stern 1993: 119-123). Of course it could be argued that they have been rather conservative in the TPA question, but as soon as legislation is in place the companies must adjust use the Internal Market provisions, something that the industry now seems to be realising. Furthermore, it could be argued that even though regulation has been proposed by the Commission, member states have always succeeded in modifying the Commission proposals. Integration has stagnated before, and even if the Commission succeed to accomplish the Internal Market on energy, it can not happen without the full participation of governments and the industry. The Commission has shown in the past that it might be necessary to concede if opposition is too strong, something that could happen in the light of the apparent ideological opposition of France and Germany. Finally, when it comes to shifts in political expectations, it should be noted that energy companies seem to rely on both levels of government for influence. They cooperate closely with their national government domestically and at the EU level, but at the same time they are very much involved in EU decision making (Interview 2). The result is that expectations have not *shifted* from the national to the EU level, rather they complement each other.

With the above mentioned considerations in mind, it must be emphasised that the Commission is stronger than ever when it comes to the energy field. This is partly due to a successful tactic of establishing energy as part of the Internal Market, and thus the ability to use competition legislation, and partly due to a shift in political expectations to the Commission as the initiator of energy policy. If the Lisbon Treaty is ratified it is hard to see that the Commission will lose influence over the internal aspects of energy, even with member state modifications. However, things are more uncertain in the external dimension. As mentioned earlier, the Commission has been quite successful in the past of using issue linkage (Matlary 1998: 120). The second part of the analysis will shift the focus to the linkage between the Internal Market, climate change and energy security. This might be an avenue for the Commission to move beyond the Internal Market in the agenda setting scope.

5. Case two: The energy policy triangle

This section will assess the increased use by the Commission of issue linkage in the energy sector to get support for a more comprehensive approach towards energy policy. The EU is developing an energy approach called an Energy Policy for Europe (EPE). There are great tensions in this policy area, partly because the Commission has a limited legal basis for dealing explicitly with external energy relations (Haghighi 2007: 67-74). On the other hand, the global implication of energy policy makes it easier to legitimise a coordinated effort than the case for geopolitical external energy relations (Matlary 1998: 149-50). Furthermore, in the proposed Lisbon Treaty there is an explicit legal recognition of the role of the EU in the internal energy market. In addition to this, there seem to be high support for the EU to talk with one voice in relation with producer countries such as Russia (Interview 2,3,5,8). This is why I will argue that even without the recognition of a coherent energy approach the Commission is using issue linkage actively to achieve a *de facto* common energy policy for Europe. The following section will provide a very brief overview of early Commission initiatives in the energy sector.

5.1 The early phase: Energy Charter Treaty and the environment

The Commission had a cautious approach to external energy relations in the early phase after the Single European Act. There was no mentioning of an external energy dimension to energy in the 1988 Commission Working Document that sparked energy liberalisation (Haghighi 2007: 62). After the fall of The Soviet Union, there was a notion that the EU needed to act to strengthen its position towards the huge Russian oil resources, and it was in this climate the Charter Treaty was established. The goal of the Treaty was to establish a framework for energy trade, transit and cross-border investments (Haghighi 2007: 187-198). It was signed by 50 countries, including Russia, in 1991. I will not go into detail about the provisions of the Treaty or its level

of success, but rather look at how it was created.⁸²⁸³ Even as a predominately trade related treaty, security of supply aspects are important with regard to investment and transparency in producing countries (Haghighi 2007: 189). This makes the Energy Charter Treaty the first important common external energy policy domain for the EU. The Commission took a leading role in drafting this Treaty (Haghighi 2007: 187-8). The Energy Directorate of the Commission took control in an apparent deadlock among the member states. France showed little interest, while the UK and Germany were mostly concerned about its location (Matlary 1998: 116). The Commission became the leading policy maker, and conducted talks with Russia about the content. This way, the Commission was able to use its initiating role to decide what would be content to be discussed by member states (ibid). In 1995 it was decided that the Treaty Secretariat would be in Brussels, something that could further enhance the role of the Commission in forging international energy policy under the Charter (Matlary 1998: 117).

In 1990 it was acknowledged that energy and the environment should be coordinated. The Commission soon took the initiative to propose a carbon tax in 1991.⁸⁴ The stabilisation of carbon dioxide emission had been clarified the year before the first joint energy and environment Council in 1991, and the proposal of the Commission would in fact be the first EU tax. The Commission took the leading role in merging energy and environmental policy, as well as in developing a framework for the Carbon tax (Matlary 1998: 68-71). Even though the tax was difficult to implement because of member state resistance, it can be considered an important step in the creation of an EU environmental policy (Matlary 1998: 65-71). The Commission was very much concerned with completing the Internal Market until the mid- 2000s.

⁸² For a detailed analysis of its provisions see Haghighi (2007: ch. 5).

⁸³ Some people now view the Charter Treaty as obsolete: *"It is a growing acceptance that the Energy Charter Treaty was written for a particular time and in a particular context, and while some of the issues surrounding it still exists ultimately the Russians are not going to ratify the Energy charter Treaty, and we have to find other ways to fulfil the same objectives."* (Interview 4)

⁸⁴ Commission (1992): A Strategy to Limit Carbon Dioxide Emissions by the year 2000.

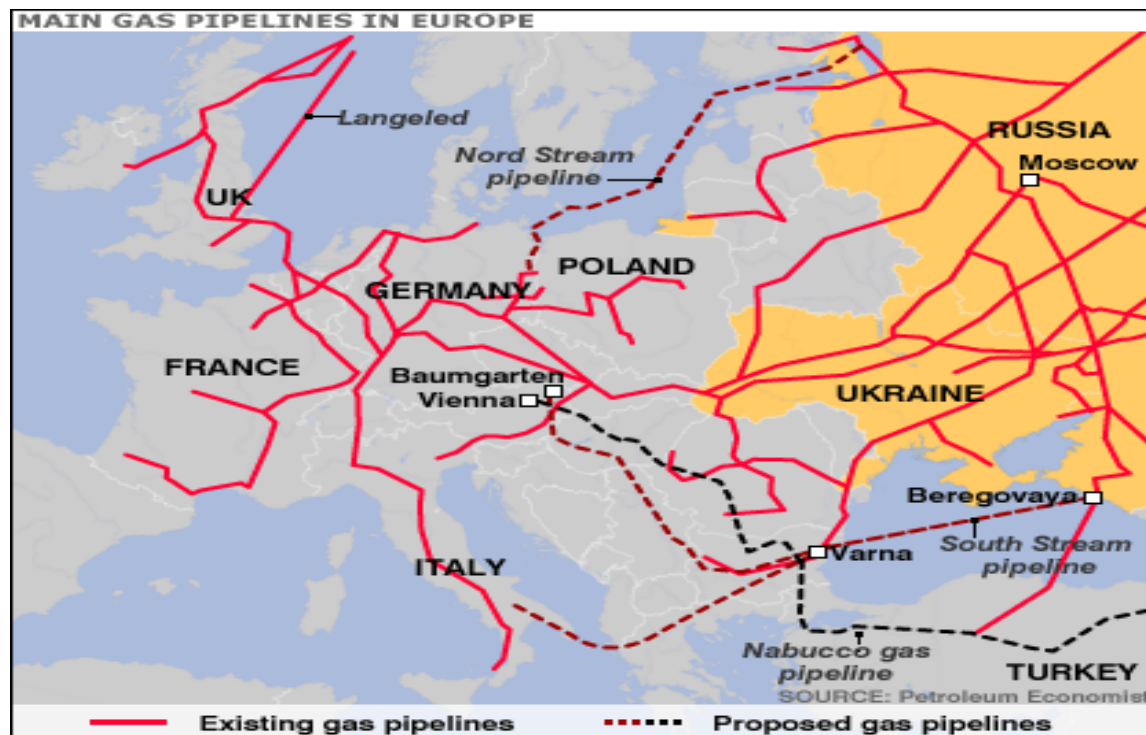
(Haghighi 2007: 171-186). However, the last few years the role of Russia and climate change has strengthened the position of a comprehensive EU energy policy.

5.2 Security of supplies

In January 2006 the Ukraine gas crisis sent shivers of cold war feelings across Europe. 80 % of gas imports from Russia to the EU are transited through Ukraine (Stern: 2006).⁸⁵ In the winter of 2005-6 this dependency became a problem as Russia decided to punish Ukraine in an apparent price dispute. Russia has always had a two price policy between Western European markets and domestic and “neighbourhood markets” (Spanjer 2006). Even with “friendly prices”, Ukraine had for a decade had huge debts to Gazprom and Russia. However, this was about to settle before the “velvet revolution” in Ukraine in late 2004. In 2005 the policy climate between the countries was hostile, and Russia started to review its dual price policy. What followed was a heated price dispute between the two countries. Furthermore, it was revealed that Ukraine had “lost” a significant amount of gas that was stored in Ukraine during 2005 (Stern: 2006). This called into question the whole security of Russian surplus gas stored in Ukraine, and further worsened the price dispute.⁸⁶ By the end of 2005 Ukraine was only prepared to pay about half of what Gazprom demanded for deliveries to the country, something that triggered a four day stop in deliveries to Ukraine (Stern: 2006). This dispute is still not settled, even though deliveries are made at the moment. The impact for the EU of the four day supply stop was shortfalls in deliveries to several countries (ibid).

⁸⁵ See figure 5.2 for an overview of existing and proposed gas pipelines in Europe.

⁸⁶ There were of course many issues at stake during this dispute, since virtually all agreements on gas between Russia and Ukraine were in effect declared void. For a detailed analysis see: Stern (2006): The Russian- Ukrainian gas crisis of January 2006.

Figure 5.2**Main gas pipelines in Europe⁸⁷**

This was a wake up call for the European Union, even if it can be questioned whether this dispute was a political statement or merely a price dispute. All CIS countries except for Belarus faced price increases in 2006. Furthermore, no political demands were made from Russia during the crisis, it all related to the price increase (Stern. 2006). Even if the cutting of gas was a political gesture towards importing countries, the lasting result of it was that the EU saw how vulnerable it is when Russia decides to cut supplies. A representative of the European Council put it this way:

“ We started looking (...) at the question of energy as a driver of foreign policy some time in the middle of 2005.(...) It would be wrong for me to say we foresaw the gas crisis(...) It was badly managed, that’s probably the way to put it. (...) That was a bit blown out of the water in January 2006 when there was a clear use of energy as a power tool. And it made us refocus a bit about what we were doing and how we were doing it.” (Interview 4)

⁸⁷ The picture is taken from BBC and Petroleum Economist:
http://newsimg.bbc.co.uk/media/images/44470000/gif/_44470431_russia_pipelines_416_1.gif

This was also the case for the Commission:

“(...)In the wake of the Ukrainian gas crisis, The commission has seen a lot of criticism. (...) I think that much in response to this criticism, the Commission has sought to be somewhat more assertive on the external front, but they still have a problem in that they still don’t have a legal base to make proposals.” (Interview 4)

Surely, the Commission had also been dealing with external policy considerations in the past. In several communications and papers from 1995- 2002 the Commission stressed the importance of energy security, especially in the 2000 Green Paper “Towards a European strategy for energy security”.⁸⁸ Even if these “soft law” proposals referred to the external dimension of energy supplies, the main focus of the Commission was to complete the Internal Market (Haghighi 2007: 181). Security of supplies has predominately been dealt with by member states at the bilateral level. Therefore it was not until the aforementioned gas crisis that the Commission initiatives on an external dimension were thought to be sufficiently credible (Geden et al: 2006). This reluctance relate to the sensitivity of energy supplies to national security, something that member states will not give up easily to a European institution (ibid).

The Heads of State officially recognised the need for a coordinated effort in the external energy sector in the Hampton Court Council meeting in 2005. However, the member states did not trust the Commission completely to forge such a policy. In stead it was decided that the coordinating efforts would be made in cooperation between the Commission and the High Representative of the Council, lead by Javier Solana (Geden et al 2006: 11-12). They issued a common report in June 2006 stressing the need for energy partnership with third countries, improvement of transit infrastructure, promote climate change mitigation and coordinate stock reserves of

⁸⁸ For a detailed discussion about White Papers, Green Papers and Communications in 1995, 2000, 2002 and 2003 see: (Haghighi 2007: 156-186)

energy source.⁸⁹ The main principles of the coordinated policy would be well-functioning markets and diversity of supply routes (Ibid).

5.3 Energy and climate change

With these initiatives, the Commission had a momentum to flesh out concrete measures, even without explicit recognition of competencies. In 2006, the Commission issued a green paper calling for a one voice policy and sustainable energy developments.⁹⁰ The Green Paper lists the following policy priorities: completing the Internal Market, solidarity between member states, a sustainable energy mix, an integrated approach to climate change, a European energy technology plan and establishing a coherent external energy policy. Compared to previous policy initiatives from the Commission there are two important novelties to highlight here: climate change and external energy policy. The first element is the linkage of climate change to the Internal Market and energy security. The Green Paper highlights the ongoing debate about climate change and calls for a coherent green house gas policy, cutting emissions with EU wide goals and further developing the Emission Trading Scheme (ETS). In relation to an external energy policy, the Commission calls for action to ensure diversity of supplies, energy partnership with producing countries and to create targeted measures to react to supply crisis. Furthermore, it calls for an integration of energy into other policies with an external dimension. The EU should act with one voice when it comes to energy and climate change on the international arena. This policy document is very interesting because the Commission is now very clear on the “Europeaness” of energy policy. The focus is on the need for a truly European policy and a common voice, and there are proposals for a European Regulator to regulate continental gas grid and also mentioning of a European Energy Supply Observatory (Haghighi 2007: 171-7). The newfound “Europeaness” of an

⁸⁹ Commission and High Representative (2006): “An external policy to serve Europe’s energy interests”

⁹⁰ Communication from the Commission (2006): “A European Strategy for sustainable, competitive and secure energy”.

encompassing energy policy is guided by the triangle of the three policy areas, something that was confirmed by a representative of the Commission in an interview with the author.

“There has been an awareness rising about several areas which are dependent of each other, (...) It is some kind of triangle of energy security (...), economic development and climate change. (...) Usually we look at energy security only, but you have to look at this triangle(...). (Interview 1)

About the relation between the internal and external dimension of energy policy:

“If you are talking about the Internal Market liberalisation, it’s an important issue to promote the triangle between security of supply, efficiency and climate, and economic development. But if you are talking about the external relations, you see that a one voice policy is definitely needed.” (Interview: 1)

The issue linkage can not be stated clearer. Sometimes it seems a bit confusing which are is the responsibility of whom, but the Commission is clearly trying to expand its competencies into all areas of energy policy. (Haghighi 2007: 183). This is thus a very difficult policy area to assess. Most people seems to agree that the right to chose energy mix will always remain part of the national competence (Interview 4,5). Thus it is interesting to see the broad support the Commission gets for its efforts to speak with one voice internationally. A representative of the German government says:

(...) Commercial contracts between companies, but political talks are involved as well, and there it is better that the EU stands together and acts as a whole. (...) I think generally agreements are stronger when we act together” (interview 5)

Of course the German government is here talking about a unified policy in among member states, and not about letting the Commission deal with this issue independently. This is also the reason why member states has agreed to let the High Representative of the Council deal with the external dimension of energy as part of the Common Foreign and Security Policy (CFSP) (Geden et al 2006: 11-12). Still, there is now an explicit recognition that all aspects of energy policy should be dealt at

the Community level. In this respect the pressure towards climate change policy is also an important tool for the Commission.

There has been an intensified issue linkage policy by the Commission since 2007. The energy and climate change packages are of course independent legislative packages. As discussed, the Energy Package deals with directives concerning the gas and electricity markets, as well as the establishment of a European Regulator. The climate change package entails provisions for a common approach to reduce greenhouse gas emissions with 20 % by 2020 and to further develop ETS. I will not go into greater detail about the actual proposals, but focus on how the Commission has now piled these proposals together.⁹¹ The integration of the two packages was announced 10 January 2007 and the Commission issued a press release on an “integrated climate change and Energy Package to cut emissions for the 21st century”. Commission President José Manuel Barroso said:

"Today marks a step of change for the European Union. Energy policy was a core area at the start of the European project. We must now return it to centre stage. The challenges of climate change, increasing import dependence and higher energy prices are faced by all EU members. A common European response is necessary to deliver sustainable, secure and competitive energy. The proposals put forward by the Commission today demonstrate our commitment to leadership and a long-term vision for a new Energy Policy for Europe that responds to climate change. We must act now, to shape tomorrow's world." (Barroso: 2007)⁹²

At this time the Commission had launched a new slogan in the energy sector: a sustainable, competitive and secure energy supply. In 2007 the Commission produced a leaflet to explain the EU strategy for a “new Common European Energy Policy.” The policy includes for the EU to take global action and to speak with one voice in

⁹¹ The policy is explained in: Commission (2008): *20 20 by 2020 Europe's climate change opportunity*.

⁹² Commission press release (10.1.2007): “Commission proposes an integrated energy and climate change package to cut emissions for the 21st Century”
<http://europa.eu/rapid/pressReleasesAction.do?reference=IP/07/29&format=HTML&aged=0&language=EN&guiLanguage=en>

international negotiations on energy. Furthermore, the EU should make better use of what the Commission calls “the new internal energy market”, for which it states that there are still steps to be taken to achieve a fully competitive market. Regarding climate change the leaflet targets energy efficiency, renewable energy sources and new technology as steps to be coordinated. In addition the leaflet calls for more solidarity in the case of crisis.⁹³

The climate change package was released 18 January 2008, completing the objectives set out early in 2007. With this the Commission had presented the whole array of legislative proposals on climate change and energy, so it could be ready to be treated in the 2008 energy and environment Council in Brussels. In these proposals there were no specific provisions for external energy policy, but in addition to these highly complex proposals the Commission and High Representative of the Council issued a policy paper linking climate change and energy security. This was done right before the Spring European Council in which the Heads of State meet to suggest future priority areas for the EU. The paper focuses on threats posed by climate change to international security. This includes conflict over resources, economic damage and tension over energy supply. To better address these issues the paper proposes to enhance capacities at the EU level to intensify EU research programs and further develop crisis management mechanisms.⁹⁴ The European Council is the highest authority of the EU, and policy recommendations from this forum are extremely important (Lewis 2007: 158). The next section will review the interaction between the “soft law” approach of the Commission and the legal recognition of the European Council.

⁹³Commission (2007): “*Energy for a changing world. An Energy Policy for Europe – The need for action*” http://ec.europa.eu/energy/energy_policy/doc/2007_03_02_energy_leaflet_en.pdf

⁹⁴ High Representative and the European Commission (2008): “Climate change and international security”

5.4 Agenda setting and soft policy instruments

The Commission has a very important role as agenda setter in the energy field. This is no minor power, and the use of “soft law” proposals by the Commission should not be underestimated. “Soft law” proposals are understood as Green Papers, White Papers and Communications from the Commission that provide general policy proposals for the member states and the Parliament to consider.⁹⁵ These are not actual policy proposals that are by law classified as regulations, directives, decisions, recommendations and opinions under Article 249 of the EC Treaty (Haghighi 2007: 178). The Green Papers are “intended to stimulate debate and launch a process of consultation at European level on a particular topic” (Haghighi 2007: 177). The result of the Green Paper is usually a White Paper which includes concrete policy proposals for action. If these proposals are welcomed by the Community institutions, they can be adopted as prioritised policy areas for the EU. Sometimes the Council and Parliament adopts Resolutions on the Papers, and sometimes they do not. Furthermore, these papers do not constitute any rights or obligations upon the member states, and are thus not politically binding. The same goes for Communications, which are also general comments from the Commission, but they do not necessarily lead to concrete policy proposals (ibid).

⁹⁵ See table 5.4 for a list of soft policy proposals by the Commission

Table 5.4*List of soft policy proposals by the Commission in the external energy dimension 1995- 2008⁹⁶*

1995:	<i>White Paper on an energy policy for the European Union and external security of supply (Commission)</i>
2000:	<i>Green Paper: Towards a European strategy for the security of energy supply (Commission)</i>
2002:	<i>Communication on the Internal Market in energy and coordinated measures on the security of energy supply (Commission)</i>
2003:	<i>Communication on the development of energy policy for the enlarged European Union, its neighbours and partner countries (Commission)</i>
2006:	<i>Green Paper on a European strategy for sustainable, competitive and secure energy (Commission)</i>
2006:	<i>Communication: External energy relations: from principles to action (Commission)</i>
2006:	<i>An external policy to serve Europe's energy interests (Commission and High Representative of the European Council)</i>
2008:	<i>Climate change and international security (Commission and High Representative of the European Council)</i>

These policy proposals have significance for Community priorities. Even if the Green papers do not have a legal effect they are used as guidance for future regulation. It is used by the Commission as an alternative to legislation, when member states cannot agree on Community action. This way it functions as a substitute for documents which has legal effects. Most importantly, these documents most often turn out to become Community law after some time. The area of energy security is here very important where consensus is very difficult to reach. The numerous “soft law” documents that have been published by the Commission in the energy sector show persistence from the Commission in setting the agenda in the face of member state resistance. It is as if the Commission is issuing these recommendations while the

⁹⁶ Haghighi (2007: 155-181) discuss the each of these proposals in more detail, except the last three in this table. The two last proposals are called “Papers” and are issued by the Commission and High Representatives jointly. See Geden et al: 2006 for an explanation of this arrangement.

actual recognition of Community action is pending (Haghighi 2007: 180). The density of soft law proposals from the Commission in the field of energy is increasing, and this gives uncertainty to the legal justification of them. It is not given that more soft law proposals will necessarily lead to more EU competencies. Still, when the Commission so frequently link the external and internal aspect of energy, the chances increase that the link will be explicitly recognised (Haghighi 2007: 183). In fact it is possible to argue that this is now about to happen. The last few years there has been an increasing interaction between the Council and the Commission on these soft law proposals, leading to a limited legal recognition of Community action in the whole spectre of energy policy.

5.5 Council recognition

The European Council is the most central policy making institution in energy questions.⁹⁷ Not only are decisions made in here, in coordination with the Parliament, it also issues policy recommendations based on proposals made by the Commission. The Commission can get “go signal” for its policy priorities and thus a legal basis from the Presidency Conclusions.⁹⁸ The merging of energy security, the Internal Market and climate change is to a great extent based on the 2006 Spring European Council recommendations. These provisions justified the previous provisions suggested in the Green Paper on Sustainable, Competitive and Secure Energy that was issued before this meeting.⁹⁹ One of the few things thing left out in the 2006

⁹⁷ The Council on energy and environment ministers legislate on their respective policy areas together with the European Parliament (except for CFSP which requires unanimity in the Council) The Heads of State meets in the European Council shortly after the energy and environment ministers, and the policy documents discussed here are all from the European Council meetings. Please note that I acknowledge the legislative role of the European Parliament and EJC, but there these will not be discussed in this thesis. See Lewis (2007) for a discussion of the role of the European Council in the EU system.

⁹⁸ As an example see: Commission (2007): “An energy policy for Europe”

⁹⁹ Commission (2006): “Green Paper. A European Strategy for Sustainable, Competitive and Secure Energy”

Recommendations was the fact that climate change policy should not have an impact on the right for countries to choose their energy mix.¹⁰⁰

Even if the 2007-8 energy and climate change packages was based mostly on the 2006 Green Paper and Presidency Conclusions, the content was further justified in the 2007 Spring European Council. Prior to this meeting, the Commission presented its integrated energy and climate change policy¹⁰¹. The result was that the 2007 European Council Conclusions endorsed an integrated climate change and energy policy, given that it respects member states right to choose energy mix:

“Given that energy production and use are the main sources for greenhouse gas emissions, an integrated approach to climate and energy policy is needed to realise this objective. Integration should be achieved in a mutually supportive way. With this in mind, the Energy Policy for Europe (EPE) will pursue the following three objectives, fully respecting Member States' choice of energy mix and sovereignty over primary energy sources and underpinned by a spirit of solidarity amongst Member States:

- increasing security of supply;*
- ensuring the competitiveness of European economies and the availability of affordable energy;*
- promoting environmental sustainability and combating climate change.”¹⁰²*

In the same document as the Presidency Conclusions, the European Council produced an annex to the Presidency Conclusion named: European Council Action Plan (2007-2009), Energy Policy for Europe (EPE). This was the starting point the Commission needed to complete the Internal Market and to coordinate efforts of energy security. In addition, this was the basis for proposals made in the climate package¹⁰³. It is

¹⁰⁰ European Council (2006): “Presidency Conclusions”

¹⁰¹ Commission (2007): “An energy policy for Europe”

¹⁰² Ibid.

¹⁰³ Commission (2008): *20 20 by 2020 Europe's climate change opportunity*

interesting to see how the Commission in this Annex got recognition for most of the policy suggestions in the 2006 Green Paper. The work that was started with this Green Paper is now being completed, hopefully within this year. The 2008 Spring European Council had a whole section dealing with climate change and energy. These provisions further strengthened the mandate of the Commission for energy and climate change policy, and furthermore it stresses the need for a “one voice policy”:

“The European Council recalls the importance it attaches to enhancing the energy security of the EU and its Member States. Whereas action on climate change and energy, the internal energy market and new technologies all contribute to this objective, work must also be vigorously pursued on further developing the external dimension of the 2007-2009 Energy Policy for Europe.(...) The European Council attaches particular importance to the EU and its Member States speaking with a common voice on energy issues with third parties.”¹⁰⁴

In 2008 the European council did not have a reference to the national choice of energy mix. This means that it becomes even more unclear where to draw the line between EU and member state competencies in the external dimension of energy policy. Stakeholders interviewed in Brussels for this purpose seemed to be certain that member states would not give up competencies:

The Commission:

“I do not believe that member states will give up competencies, but if you see the Lisbon Treaty you see that the awareness is rising that it really needed an external policy” (interview 1)

¹⁰⁴ European Council (2008): “Presidency Conclusions.”

The Council:

“No I don’t think so at all. A part from anything else, when it comes to questions of nuclear energy, it will be very difficult for the Commission to find any common ground. That said, the whole question of climate change and how we will respond to it, I think is probably going to be a greater driver for energy policy than anything else” (Interview 4)

The German government:

“In the EU of 27 MS there is always some difficulty in building a common front depending on the subject more or less, but if you want to align positions for 27 countries there is always debate involved, and this is also true for energy policy and CFSP and when these two interlinks there is debate, and individual countries still have, and will have national positions.” (Interview 5)

Clearly, there is a great tension about the competencies of member states and the Commission, especially on the external dimension of energy. However, it is remarkable to see how far the EU and the Commission has come to establish a truly encompassing common energy policy. The concluding chapter will evaluate the agenda setting power of the Commission and its role to create loyalty transfers and spillover in the energy sector reviewing different theoretical contributions.

6. Comparing cases: Haas revisited

The empirical findings in the two chapters above are interesting in their own respect, but this chapter will look for linkage between them to better evaluate the theoretical predictions. It is natural to this within the framework of Haas' conditions for political integration since this is the theoretical starting point. As pointed out in the second chapter, developments in European integration theory make it imperative to evaluate the empirical findings within more contemporary approaches. More recent neofunctionalist inspired integration studies usually only pick and choose parts of the theory, rather than treating it as a grand theory (Jensen 2007: 96). The approach here will be to modify the findings before discussing the core predictions of loyalty shift and spillover. For this purpose I have chosen the approaches of multi-level governance (MLG), new institutionalism (NI) and differentiated integration because they help to clarify the core concepts of the theory. The MLG and NI approaches deal with loyalty shift and spillover, because they help identify sources of contestation between and within levels of government. Furthermore, differentiated integration is a theoretical approach that helps explain how the implementation of EU regulation is heterogeneous across the member state level even under the expansion of EU competencies. Please note that I am not trying to provide an exhaustive list of integration theories, and there are several approaches that I deem to be fundamentally different and thus do not treat here.¹⁰⁵ The main approach is neofunctionalism, and the other approaches are merely used to modify this theory within the contemporary context. The next section will evaluate the empirical findings using the approach of Haas.

¹⁰⁵ The most prominent theoretical approach that I do not study is intergovernmentalism, because I believe that the approach relies too much on governmental bargaining, missing the role of the Commission which is the core of my study.

6.1 The transfer of sovereignty and new alignments

Haas provided a comprehensive approach to establish conditions for integration (Haas 1958: 15-16). This is a three step approach, but the last step is a periodic review of the conditions in step one and two. This is why only the first two steps will be treated here, as the empirical research in this study is a periodical review of integration in this particular sector. The first step is to identify the initial position of key interest groups and governments toward integration. Then it must be established whether this position correlates with economic and political expectations or national interests. It is impossible to trace this without the Single European Act (SEA). With SEA the Commission had a greater momentum than ever before to abandon state monopolies in the energy sector (Matlary 1998: 115). This milestone in European integration created the rationale for establishing an Internal Market, including the energy policy sector. There have been numerous studies of the creation of SEA. (Andersen et al 2006: 316).¹⁰⁶ One of the most interesting explanations is that of favourable externalities. The international community experienced an unprecedented liberalisation wave in the 1980s, inspired by Thatcher- Reaganism. This climate of liberalisation was also apparent in the energy sector, largely justifying moves of the Commission to liberalise the heavily nationalised energy sector (Andersen et al 2006: 9). In this respect it is possible to argue that the Commission were not responding to local preferences when initiating liberalisation in the energy sector, rather it used a model already established in USA and the UK (Ibid). The Commission was thus arguing through an economic perspective, and using the newfound political expectations in the SEA (Ibid). This notion is strengthened by the fact that it took several decades for the EU to even consider energy as a Community policy area (Schmitter 2005: 266-7). The EU started to consider energy security mechanisms as a response to the oil crisis in the 1970s, but it was not until the Russian- Ukrainian gas

¹⁰⁶ The development of SEA is not under study here, but it did create favourable conditions for integration in the energy sector. See Moravcsik (1991) and Tranholm-Mikkelsen (1991) for contrasting views on the origin of SEA from an intergovernmental and neofunctionalist perspective.

crisis that the EU coherently approached an encompassing energy policy. Since 1995 The Commission proposed several policy measures to address security of supply issues. Even if the Commission had the right of initiative in the environment and Internal Market policy areas, they were not allowed to effectively link these to security issues that might affect the right of member states to choose energy mix. When the Russian- Ukrainian gas dispute maximised the security alertness of EU countries, the Commission could more easily forge EPE, even if the content of it is not yet clearly comprehensive. Certainly favourable external trends and shocks seem better fit to explain growing interdependence in the energy sector than purely regional developments (Ibid).

The fact that integration was sparked by external precedence and warranted in the SEA was not enough to convince the industry and decision makers in central member states. Except for the UK, energy policy integration was not initiated by national preferences. The empirical findings clearly show how much resistance the Commission experienced in the energy sector. Jonathan P. Stern summarised the reception of the 1988 working document on the energy sector this way:

“From the publication of the working document in 1988, gas companies and producers combined to resist any move towards the introduction of TPA. Attitudes towards the European Commission proposals varied from antipathy and suspicion, to thinly disguised fury and contempt”
(Stern 1992: 73)

Clearly, even if the international environment was favourable to liberalisation of the energy sector, the regional setting was not. The resistance of the key interest groups and governments to integration seems to be a result of security of supply concerns. There were tacit agreements between governments and the industry to let transmission companies handle supply and demand and thus prices for security of supply concerns (Stern 1992: 1-10). When the same actors loudly voiced security concerns to oppose liberalisation, it was rather because the issue surfaced than that the traditional system was necessary more secure (Luiciani 2004: 4). The fact to the matter was that key actors remained happy with status quo. The role of the Commission was thus to drive

through the principle of liberalisation, since it was so fiercely opposed by central member states (Andersen et al 2008: 12-14). In this respect EU competencies in the energy sector seems to be driven by the central institution itself rather than based on the preferences of national interest groups. That said, the SEA created the favourable conditions necessary to give the Commission incentives. Also necessary was the examples set in USA and the UK for liberalisation in the energy sector, making the policy area more vulnerable to Internal Market considerations (Ibid).

The initial transfer of sovereignty from member states to the Community in the energy sector can be labelled as Commission driven under favourable circumstances. This relates to both cases, as with both the internal and external aspect, Community competencies have been opposed, but made possible due to externalities. One important difference to note between the cases is that Internal Market provisions have undergone persistent resistance from several member states. In the case for the creation of EPE, the transfer of sovereignty has not been so heavily resisted by member states after the Ukrainian gas crisis. The only remaining obstacle for creating EPE was in the external security area, a policy area that has been increasingly sanctioned for the EU, as shown in the last chapter. In fact, many stakeholders blamed the Commission for being too passive prior to the gas crisis in 2005-6 (Interview 4). In addition there is a recognition among stakeholders that the EU need to speak with one voice internationally to look stronger (Interview 1,2,3,5). These considerations suggest that the transfer of authority came out of economic reasons in the case of the Internal Market, and more of national security interests in the case for EPE.

The second step of Haas' evaluation relate to the shift in position after the advent of central decision making (Haas 1958: 15). The key task is to establish where shifts in loyalty stem from: *"If patterns of identities, convergence or opposition are in evidence, the effort must be made to determine whether they originate at the national level or the "supranational" level"* (Haas 1958: 16). Classical Neofunctionalism would predict that the commission would take a lead role in the integration process. As long as the central institution is in place it will be inherently expansive (Rosamond

2000: 57-9). There is no doubt that the Commission has had this role in the energy sector. In the Internal Market it sparked the integration off with the 1988 working document on the Internal Market (Stern 1992: 55-56), while in the external sector the Commission has made several consistent efforts to create a coherent approach (Haghighi 2007: 155-177). With its multi-national staff and agenda setting power, the Commission works far beyond national interests of single members (Egeberg 2007: 144-5). This implies that as soon as the Commission is given competencies it should be expected that it will act inherently expansive to enhance EU level decision making. This further strengthens the notion of political spillover, a process that is initiated by the central institutions and certain interest groups, rather than a process of automatic spillover (Jensen 2007: 90-92). Both cases confirm this notion. The method of proposals and concessions in the Internal Market development indicate that the Commission maintain the role as driver in a political spillover process. The same goes for the EPE, where the Commission use issue linkage to enhance competencies from the existing legislative basis of the Internal Market and environment.

There are a few concerns that modify the notion of political spillover. In the first case, opposition has been consistently strong and voiced. Industry and decision makers have internal, external and ideological concerns about the process of integration. Schmitter (1971) and Lindberg (1966) explored the idea that spillover could be deterred and even reversed if integrative incentives are insufficient (Rosamond 2000: 63-65). The diminishment of national state competencies could trigger unbearable tensions within the member states, and create calls for “retrenchment” or “spillback” of competencies. Certainly, at the moment there is no evidence of spillback of EU energy competencies, rather the opposite in both cases. Still, the strong ideological opposition identified in Germany towards the Energy Package indicates that national decision makers are far from content with the drive of the Commission for integration. In the external dimension the role of the Commission is diminished by the enhanced role of the Council Secretariat and High Representative (CS/HS) (Egeberg 2007: 141-3). Even though EPE is an established policy in the EU institutions, member states would not give the Commission sole responsibility for the external

energy policy dimension. Still, the Commission works closely with the HR, and they issue policy papers in together. This gives the Community increasing competencies in the external energy sector as part of the CFSP (Larsson 2007: 20-25). The interaction between “high” and “low” politics is an important tension in energy decision making. This relates to the debate of level and scope of EU competencies, as the level of decision making can be constrained by its scope. This could happen both as a result of intergovernmental features in the EU system and constraints in the national system. Both circumstances modify the notion of loyalty shift and spillover.

6.2 Level and scope

To understand the process of integration more clearly it is important to separate between level and scope of integration. Inspired by neofunctionalism, Tanja A. Börzel (2005) discussed the degree to which different policy areas in EU decision making has been integrated. In her study of EU treaties she traced the level of competencies in different policy areas and the scope of the decision making procedures (Börzel 2005: 219). This way she separate between decision making levels in which the formal competencies lie and the way the decisions are made with regard to member state influence. This distinction between level and scope is interesting when comparing the two cases, because it reflects the nature of integration for the internal as well as the external energy policy dimension. The use of competition policy and formal recognition of energy as part of the Internal Market would suggest that it could be treated as economic politics, and thus as an EU competency in both level and scope (Börzel 2005: 221-2). Furthermore, Börzel identified a development towards greater integration in both level and scope for CFSP matters (Ibid). Since the external dimension of energy is mainly treated by the EU as a CFSP matter it would be expected that Community institutions would share competencies with the member states. The empirical findings in the two last chapters largely confirm this view. Energy was nationalised at the time of the SEA agreement, and the legal basis for energy as part of the Internal Market was not recognised until the proposed Lisbon

Treaty. The external energy policy has been established as a priority area for the EU. This is still more of an intergovernmental arrangement because the GS/HS of the Council largely maintain the responsibility.

The debate about level and scope of EU policy making shows how integration vary depending on national constraints. The fact that both policy areas have been increasingly integrated in level and scope could be used as an argument for political spillover. In the Internal Market, the Commission activism has driven through integration from almost scratch to being a Community competency in both level and scope (Börzel 2005: 221-3). This is also the case in the external dimension, where the Commission use its agenda setting power to move EPE in its direction. Also, the Commission has used a strong DG Relex to exploit functional linkages between the security of the Internal Market and external coherence (Börzel 2005: 231) Still, in the high politics area of the external energy dimension there is still more of a distinction between level and scope. With the EPE, decision making in the external energy policy is shared in level, as member states retain their right to chose energy mix. Since the Council retain decision making power, the external dimension is less integrated in scope. This is so even though external pressures have created a drive for a more unified approach to Russia and energy security in general. This shows that it is possible to have integration in high policy areas, but also that the enhancing the level of EU competencies does not necessarily precede scope of decision making powers (Börzel 2005: 231). The next section will follow this argument by looking at the national implementation of energy policy in Germany to show how the scope of integration is limited by national constraints.

The different pace of national implementation of EU energy policy makes it questionable whether the alignments are as clear cut as it may seem. Using the theory of differentiated integration as described in chapter two, it is possible use the example of German resistance to energy integration to show how country specific attributes can hamper integration. Andersen and Sitter (2008) argue that the gas market is only partly liberalised. Furthermore, they argue that not only is the gas market not fully

liberalised, but the Internal Market looks more like the gas market than the other way around (Anders et al 2008: 1). The rationale for such a statement lies in the ambiguity of EU decision making. There are few policy areas which are homogenously implemented. The idea of the Internal Market as an encompassing homogenous economic area is caught up by the reality of politics. This is especially true in policy areas which are heavily contested by member states (Ibid: 2-6). The step by step approach in EU legislation resembles a multi-speed approach to European integration in the sector. The persisting resistance of central member states indicates that the only way for the EU to reach the objective of an ever closer union is to allow member states to implement legislation with different speed (Junge 2007: 396). This includes ambiguity with regards to the introduction of TPA and the national focus of the regulatory authority. The question now is whether this can be seen as differentiated integration with the end goal of establishing common rules for all countries, or a permanent difference in policy goals between countries (Ibid: 396-8) The Energy Package suggests that the Commission wants to create a truly common market, especially when targeting Germany directly. When this is not done as easily as the Commission hoped, the nature of domestic resistance is clearly a factor to be taken into account.

German adoption in the Internal Market for energy can be characterised as autonomous. This is the case in Germany, because central demands for integration have been weak (Andersen et al 2006: 24). The “Third option” proposal can be viewed as a status quo position. Ideological and economic resistance to the Energy Package indicates that the government is content with maintaining vertically integrated ownership of the German infrastructure, and there are thus no demands from the government to further liberalise the sector (Interview 5). This is strengthened with strong incentives for the decoupling of EU policy from the national setting. The industry is perhaps even more eager to maintain status quo. German gas companies do not want a central regulatory authority with the ability to regulate German markets (interview 2, 3). Furthermore they argue from a security perspective that dissolving companies will make them weaker when negotiating gas contracts with Russia

(written reply to author). The economic arguments from the gas sector resembles that of the industry, both see the separate running of gas infrastructure as insufficient to provide necessary investments and dividends for the single operators (Interview 2). This indicates that the local pressure for decoupling in combination with weak central demand for integration creates an autonomous approach to energy policy implementation (Andersen et al 2008: 5). This realisation means that the scope of the decision making procedures for the EU can not be reduced to the economic realm of the Internal Market. This is in turn a serious limit to the idea of homogenous spillover with regard to the internal energy market. The gas market have been increasingly subject to the principle of liberalisation, but the ambiguity of the policy content reveal a tension that make it difficult to argue that the Commission has fully succeeded with its activism (Andersen et al 2008: 18-21).

In the external energy dimension there are also limits to the scope of integration and differentiated national approach to EU intervention. The discussion above indicates that the Internal Market provisions are under pressure, as Germany is taking a leading role against stronger integration. This indicates that the Commission is basing its issue linkage on a fragile ground, which is reflected in the restricted scope of external energy powers for the EU. The role of the Commission is restricted to soft policy proposals, which have only been fully taken into account as external priorities emerged. So while the the CS/ HR of the Council and the Commission has ascended the level of debate from the nation state, the scope of decision making is very much limited by national constraints. This picture is strengthened by the fact that several member states follow a bilateral track when negotiating agreements with energy producing countries like Russia (Interview 7). An example of this is the North Stream pipeline in the Baltic Sea, which was initially negotiated between Gazprom and German energy companies without taking into account the position of affected EU countries (Sander 2006: 20-22). Even though this project was later included to be a part of the “trans- European networks” of gas infrastructure, the deal was made bilaterally (ibid). Furthermore, Russia continues to push Eastern member states to opt for the South Stream pipeline in stead of the Nabucco pipeline from the Caspian

Sea¹⁰⁷ (Interview 4). The policy triangle between climate change, energy security and the Internal Market is thus not so obvious for the member states as it seem to be in the Commission.

Integration in the energy sector is identifiable, but more in level than in scope. The transfer of authority and thus new alignment towards the central EU level has made EPE possible. However, this has not come in the form of smooth spillover effects under Internal Market conditions. Furthermore, there is still a need for careful diplomacy when dealing with the Russia (Luiciani 2007: 7). This makes member states reluctant to give up their right to right to maintain bilateral relations in the energy sector (Larsson 2007: 24-26). In the internal energy market member states have different ownership structure and dependency situations, something that affect their position towards EU policy (Interview 4). The discussion between member states and central institutions about the pace and nature of integration is of essence to European governance, something that both cases are examples of. The next section will shift the focus to the interaction between the different actors and institutions to better clarify their role in energy policy making.

6.3 Governance and integration

The discussions so far has focused on the process of integration, but contemporary EU scholars are often more concerned with the “governance” perspective of the EU (Rosamond 2000: 109-110). With regard to the “governance turn” in European studies this section will move beyond integration, and study the sui generis nature of European integration. This helps to clarify the different role of the multiple actors and institutions in forging EU policy in the complex contemporary setting of the EU. The theoretical approaches for this purpose will be multi-level governance (MLG), and new institutionalism (NI). I will not go into detail about these theories, but look at

¹⁰⁷ The Nord Stream and South Stream project originate from Russian gas, while the Nabucco pipeline is a project that is made to diversify supply sources. All are still in progress of being made, see figure 5.2

some interesting perspectives relevant for how the Commission operates and is constrained by other actors. This way the neofunctional predictions will be further modified by offering more contemporary approaches to how the Commission works as guardian of the Treaties.

MLG captures the complexity of decision making authority at several levels in Europe. This is in contrast to traditional neofunctionalism that would claim that interest groups and eventually governments peak their resources to the central level to achieve highest level influence (Rosamond 2000: 51-2) . This notion needs to be modified. First of all, companies operating in the EU most often operate at multiple levels (Eising 2004: 214-16). Furthermore, functional tasks most often do not coincide with territorial boundaries (Idid). This is true for German gas companies which operate in several countries, and need to cooperate with more than one country. Since the upper level of decision making in the EU is autonomous but not supreme to the member states, neither can claim full loyalty of the interest groups (Eising 2004: 214-16). German gas companies have a tradition of governmental support for their operation (Sander 2006: 20). The other way around energy companies have largely been working in line with the government. This harmony seemed to be broken with the decision of E.ON Ruhrgas to sell of its electricity grid in February 2008:

(...) You do have large companies operating in certain member states doing bilateral agreements and being backed up by their governments. Again I get back to the decision of E.ON. I think that decision may make some governments think twice about giving uncritical support to their companies” (Interview 4)

This was an interesting turn in events, because it shows how companies act autonomously regardless of level. Still, being a single decision it is hard to conclude that gas companies will abandon their governments. Gas companies interviewed for this purpose maintain that they operate at both levels for influence (Interview 2). Talking to German gas companies gives the impression that they are very much comfortable with the how the German government works for their interests, but that they are more sceptical to the EU level decision making (Interview 2, 3). This

reinforces the view that the companies maintain a close relationship with the government, while at the same time being active at the EU level. One explanation for this could be that the companies need the EU level to coordinate multi-national operations. Another explanation is that large companies operate at both levels simply because they can. Having issue specific competence and huge financial resources, large companies can operate with a dual strategy. They are important actors in the national setting. Furthermore, their issue specific competence makes these companies valuable to the supply side of EU decision making. As an example, the Commission needs input from the industry to at best fulfil the demand side of policy making, making large companies indispensable partners (Bouwen 2004: 341-79). Put in another way:

“On average, these firms maintain more contacts with national institutions than national associations and more contacts with EU institutions than EU associations. At both levels of government, their direct control over substantial economic resources as well as their market and technological knowledge turn them into important interlocutors for political institutions” (Eising 2006: 233)

The Commission must deal with the challenge posed by multiple jurisdictions. Not all policies are best served at the highest level (Hooghe, Marks 2003: 5-6). One of the core assumptions in Multi-level governance is that governance with multiple jurisdictions is more flexible than concentration of power (Ibid). Surely, the EU officially operates with the system of subsidiarity, following the idea of governance at the best suited level (El- Agra 2007: 37-38).¹⁰⁸ This principle creates some confusion, especially regarding the tension between flexible procedures at the EU level and decision making at the national level (Ibid). In the energy sector the EU seem to have a preference for flexible procedures (Andersen et al 2008: 18-20). Related to the discussion about differentiated integration, ambiguity in the proposals of the Commission has led to confusion. One example is the difficulty with having

¹⁰⁸ The principle of subsidiarity was agreed upon in the Maastricht Treaty, and says that where the EU does not have exclusive competencies, EU level decisions should only be made if member states can not pursue interests themselves (El- Agra 2007: 37-38).

national regulators. Jonathan Stern (1998) has identified the lack of regulatory oversight as a severe limitation to EU energy legislation (Stern 1998: 98-102). Still, when national regulators are set up it must be expected that their main objective is to monitor member state markets. When the Commission subsequently proposes a European regulatory agency it creates fear and confusion among stakeholders as to whether this will infringe upon member state discretion (Interview 2, 3, 6). The Lisbon Treaty also gives contradictory answers to this dilemma. On the one hand the energy policy triangle is enshrined with a legal basis in the Treaty, but on the other hand the member states retain their exclusive right to choose energy mix.¹⁰⁹ Again the friction between EU coordination and national sovereignty create ambiguous policy outcomes. This illustrates how difficult it is for the Commission to balance legislation in an environment of multiple jurisdictions and loyalties.

Another tension for the Commission to deal with is whether to adjust to issue specific jurisdictions or have layers of decision making in a general purpose fashion (Hooghe, Marks 2003: 8). The contradiction relates to the role of external spillover effects, which needs coordination because policy option in one jurisdiction might have effects in other policy areas in positive or negative ways. There are two ways of dealing with this, either by limiting the number of jurisdictions or limit interaction between the policy areas. The first approach can create more durable architecture and are more common in federal states. The second option is more common at local levels, as a functional solution to governance (Hooghe, Marks 2003: 13-15). The EU Treaties have increasingly included soft coordination methods and opt out clauses in some policy areas (Junge 2007: 396-8). This means that some policy areas are less integrated than others and on that some countries lag behind in areas where others are integrated (Ibid).

¹⁰⁹ Treaty of Lisbon: Article 176A, section 1 and 2

I would argue that in the EU pillar system only the Internal Market resemble a general purpose jurisdiction, subject to supranational law. Issues concerning social services, foreign and justice affairs would resemble more issue specific jurisdictions, because policies are treated separately through interstate coordination and soft policy mechanisms. These are tensions that are difficult for the Commission to deal with when establishing EPE. The Commission seek to limit the number of jurisdictions in the internal energy market while at the same time dealing with issue specific jurisdictions in the external sector. It becomes blurry when the Commission uses issue linkage between a policy area that is treated as part of the Internal Market and areas that are not recognised as part of it. And it becomes even more unclear when countries such as Germany actively seek to maintain sector specific peculiarities even in the Internal Market. In addition the Commission has allied with national regulators in specific Internal Market sectors, bypassing the national governments (Egeberg: 2008). This further complicates the application of general purpose jurisdiction, such as an encompassing energy policy. It could be argued that one response by the Commission to handle this has been to use issue linkage to apply external spillover effects in the foreign policy sector, calling for more coordination (Börzel 2006: 230-231). Still, the external constraints upon member states mandate them to be act in their own interests (Haghighi 2007: 103-105). The strong opposition to several aspects of EPE would indicate that the Commission still have work to do to find a balance between the multiple forms of governance in the EU system and national level. The next section will follow up on this and look at institutional features of the Commission in general which contribute to shape the way it addresses problems of complex governance.

New institutionalism is gaining momentum in contemporary EU studies. The approach is also part of the “governance turn” in European studies, and like MLG it focuses on the political process rather than the degree of integration (Rosamond 2000: 105-22). It is interesting to look at how institutions can shape norms, especially given the focus in this study on the role of the Commission as a driver of integration. Haas (1958) looked at the ideal role of the Commission as an institution where actors

develop supranational ties, and shape the value of governments and interest groups (Haas 1958: 151-161). The contemporary Commission operates as a mediator between the national and supranational level, because Commissioners are delegated from member states to perform supranational tasks.¹¹⁰ Increasingly, the role of the Commission is becoming more supranational than merely an entrance point for the member states into the EU administration (Egeberg 2007: 140). This could partly be explained by the institutional features of the Commission. Firstly, the Commission is a vessel of European norms that shape the preferences of actors (Rosamond 2000: 118). Institutional features, with a large life long dedicated European staff shapes an identity that heavily modifies the national outlook of the Commissioners (Egeberg 2007: 149-50). This also relate to the role of the Commission as the guardian of the Treaties, which mandates a monitoring role over the whole EU project (Ibid 140-1). Secondly, The Commission is ideally an arena for positive-sum bargains between the EU actors. As a supranational institution the Commission can intervene between actor preferences policy outcomes (Rosamond 2000: 114). This way of mingling interests from member states, political parties and civil society is best illustrated by the extensive consultation process that the Commission conduct before every legislative proposal.

However, this positive outlook is not as clear cut as it might seem. Christiansen (1997) identified several internal contradictions and constraints in the institutional features of the Commission. The Commission is an exceptional institution that operates between politicisation and bureaucratisation. This tension relate to the fact the Commissioners have a dual role in being nationally politically appointed officials with a supranational bureaucratic mandate. The Commissioners carry on the national traits from the member states they are appointed from, and a large proportion of its staff is seconded and recruited from the nation civil service (Christiansen 1997: 82-

¹¹⁰ After an internal reorganisation of the Commission during the Prodi Commission the Cabinet of each Commissioner was made less dependent on national civil servants. After the reform at least half the staff should be recruited from within the Commission. In addition it must consist of at least three nationalities and the Deputy Head of the Cabinet must be of a different nationality than the Commissioner (Egeberg 2007:145-6).

85). This adds to the complexity of the internal arrangements; because it creates friction over national priorities in different policy areas even if the Commission is supposed have collegial responsibility. Furthermore, even in “rule bound” policy areas as competition policy the Commission faces political constraints (Christiansen 1997: 79):

“In the context of the argument here this means that in the late 1980’s and up to the present the pattern of decision- making in the general field of competition policy has been less bound by the application of rules than by political bargaining” (Christiansen 1997:79)

This brings us back to the complex set of interests working with and within the Commission towards the EPE. In the Internal Market DG Transport and Energy and DG Competition has taken a leading role in forging energy policy as a part of the Internal Market (Matlary 1998: 113-124). The latest example of the Internal Market approach, with the use of competition law, was the application of infringement procedures against E.ON Ruhrgas (Interview 2,3). This happened in parallel with the negotiations of the Energy Package and shows how these DGs work in combination to use existing legislation in to a policy area that is not yet decided upon (Interview 2). Still, there are at least four DGs involved in energy policy; DG Competition, DG Relex, DG Transport and Energy and DG Environment. Policy coordination between these departments is of essence to establish a common position. Interviews with Commission officials done for this thesis did confirm a coherent approach to the liberalisation stance (Interviews 2, 7). Still, the struggle for unity under threat of globalisation is something that could potentially disrupt the delicate balance within the Commission. This could especially be problematic if national sentiments challenge the viability of a liberalised system, for instance in the case of supply failure (Luiciano 2004: 2-8).

Since the Commission often face member state resistance it sometimes uses interest group participation to bypass national interests (Christiansen 1997: 85). This seem not to have worked too well, since the industry has opposed liberalisation of the sector since the beginning. In the 1990s it tried to assemble a roundtable of industrial

participants to develop the first round of energy market directives. This stranded because of the strong resistance among industrialist (Stern 1992: 73-75). More recently, it might then be seen as a bit desperate when it uses infringement procedures against important industrial actors when not getting them to comply (Interview 2). Still, it does seem that the Commission is running a quite lonely struggle against the industry and member states with the Internal Market as the normative driver. The result so far is that the Commission has consistently driven through a normative basis for liberalisation in the energy sector (Andersen et al 2008: 18-20). This apparent ideological coherence within the Commission enhances the role of the Commission as a vessel of norms. From the NI perspective this could be threatened, especially if it gets overly politicized. The empirical findings in the two last sections clearly show how the Commission is balancing rule application with political coordination. This tension may be determining for the unity of the Commission in the future.

6.4 Loyalty shift and spillover?

The empirical findings in this thesis would suggest a case for both loyalty shift than spillover. The case for loyalty shift is identified in both cases, and it relates to the fact that decision makers and the industry “*are persuaded to shift their loyalties, expectations and political activities toward a new centre*” as defined by Haas (Haas 1958: 16). This can be stated simply by looking at the competencies of the Commission now, compared to the late 1980s. In both cases there has been a dramatic increase in recognition for Community action. This is especially the case in the Lisbon Treaty, which is agreed upon by all EU institutions. Not only is the internal energy market recognised as part of the Internal Market, even external solidarity aspects are stated as Community responsibility. This is also stated in the European Council Conclusions of 2007 and 2008. Furthermore, all stakeholders that were interviewed for this thesis confirmed that there has been a radically increased focus on energy policy at the EU level. Stakeholders from the German side also supported the notion of a “one voice” policy for the EU abroad.

The next question is whether these loyalty transfers were initiated by the Commission or national interests. The discussion in this thesis suggest a successful tactic of “concede and propose” done by the Commission in the case for Internal Market integration. This way, it is possible to argue that the both loyalty shift and spillover was driven by Commission. This is further strengthened by the fact that central member states have resisted integration, but in the end agreed to liberalisation measures. With help from a few member states, most notably the UK, and the ECJ the Commission has driven through an impressive restructuring of European gas market. The tactic of “capturing” the opposition with infringement procedures and gradual radicalisation of liberalisation measures seems to have made it difficult for member states to resist. Furthermore, with issue linkage the spectre of energy policy is presented in package deals. This enhance the chance of the Commission to succeed against opposition, especially because “log rolling” like this makes the legislative packages almost irreversible (Schmitter 2005: 266).

The spillover thesis does not seem to hold as strong, especially with the divergence in political sanctioning of the internal and the external dimension. Even though the Commission has been a constant driver of integration in both cases, the two areas diverge with respect to externalities. The Commission has been quite successful in driving integration in the internal energy market, but far less so in external energy dimension. It must be recalled that the Commission made several proposals between 1995 and 2004 to include external considerations in the energy policy. This was not recognised until external conditions were favourable. Two alternative approaches to the automatic nature of spillover should be mentioned. Firstly some neofunctionalists would advocate the need for “cultivated” or “guided” spillover by an inherently expansive supranational institution (Rosamond 2005: 244). Certainly it would be possible to claim such a role for the Commission. In both cases the Commission has been pushing for more integration, and it does seem unstoppable in doing this. This aspect of policy expansion from an agenda setting perspective should not be underestimated, but neither should external conditions. The idea of guided spillover is difficult to assess if it can only manifest itself when there is political will for it. This

is why I would argue more for the necessity of background conditions to facilitate integration. Phillippe C. Schmitter (2005) argues that outcome of integration in a specific policy area is dependant on the mix of actors, diversity of interests, convergence in strategies, interdependence of issue arenas and degree of knowledge (Schmitter 2005: 260) This indicates that there is no given results even if obligations are formalised. The diversity of interests in the external energy dimension makes it difficult for the Commission to establish competencies in the choice of energy mix, even though the Commission is trying to establish interdependence through issue linkage. In the Internal Market, it seem as the Commission has been more successful in unifying the diversity of interests. This could better be described as a process of “concession and proposal” by the Commission than s a process of automatic spillover. Haas also saw the tension between spillover and the political process:

“Haas showed how there was an inherent tension between (a) the logic of spillover and the attendant presupposition of the politicization of the integration process and (b) the continuing emphasis on integration as a process inspired by short- interest fulfilment and shaped by “muddling through” rather than grand designs and dramatic political acts” (Rosamond 2005:249)

Furthermore, Joseph Nye (1971) argues that specific background conditions need to be present to accomplish a positive attitude towards integration (Rosamond 2004: 71-71): (1) There must be perceptions of equity in the benefits of integration, (2) There should be common perceptions of external threats and policy action to remedy them, and (3) The cost of integration should be low or exportable. In the case for creating EPE these are important consideration. The Commission only got recognition for an external policy agenda after the Russian- Ukrainian gas crisis. This is also true with climate change, it has been an issue for many years, but the combination of enhanced climate change awareness and the gas crisis made it more obvious that the EU faces external threats which need Community action. Still, Community action is not given if member states perceive the cost of giving up the right to chose energy mix as too high or unequally beneficial. Furthermore, the difficult “muddling through” process in the Internal Market liberalisation, highlighted in the first case, shows that it is difficult for

the Commission to push integration in an area where member states perceives costs as high.

The case for loyalty shift and spillover is further limited by the complex features of modern decision making. It can not be argued that integration in the energy sector has been a one way street. Multiple jurisdictions dealing with energy policy has made it difficult for the Commission to manoeuvre the political spillover in any definite direction. Political integration in the energy sector remains more visible in level than in scope. The energy sector remains heavily constrained by intergovernmental features of the external energy policy and the national implementation of the internal energy market. Even when there are functional linkages between economic, political and ideological goals, as with the “energy triangle” the Commission is faced with external spillover effects that mandate nationalistic interpretation. This is especially true with the political relationship between Russia and central member states. These considerations make it more difficult for the Commission to apply supranational hierarchical arrangements for the whole energy sector, and forces through a more issue specific approach to energy policy. Dealing with several sources of authorities and national considerations is part of EU reality, and clearly limit spillover and loyalty shift effects. This is further enhanced by internal constraints within the Commission. In the energy sector the Commission has been fairly coherent. But the above discussion of the institutional features of the Commission challenge the idea of the Commission as a vessel of norms. If loyalties are not coherent within the Commission, as could be the case with supply failure, it might be difficult to maintain a drive for further integration. To limit the EPE should be developed to better ensure that solidarity mechanisms are in place if a crisis unfolds (Luiciano 2004: 15-16). In any case it is important to look at how internal developments within the Commission might affect the future of EPE. This would be a recommended priority for further research on this topic.

At present the Commission is enjoying agenda setting power in the energy sector, which makes it a powerful institution. Still, this study shows that the Commission is dependent on explicit recognitions from member states to follow its policy. A representative of the Council put it this way:

“They (The Commission) will continue to have difficulties when what they propose goes into the CFSP area. And certainly there have been some suggestions from the Commission which in my view will not even go beyond the energy working group in the Council, because some of the proposals are so far behind what the member states are prepared to let them do” (Interview 4)

This suggests that there must be a momentum for Community action for the Commission to succeed. The case with the Internal Market debacle shows that it is difficult to drive integration when there is a lack of background conditions for doing so. The same goes for the EPE policies, where the Commission only got recognition based on external events. The history of energy policy gives the same idea; integration was only possible in the wake of the Internal Market, and not as a result of automatic spillover from ECSC. Still, the cases studied in this thesis reveal a few things about the Commission which has helped to create a shift in political expectations from the national to the Community level: Firstly, it has been very persistent as agenda setters. The Commission can be labelled “inherently expansive”, and thus persistently propose further integration in the face of opposition. Secondly, it uses existing legislation to push for new competencies. This has been especially true with competition policy. A representative of the German gas industry said:

(...) (the legislative process is) turned upside down because they were told by the Commission a couple of conditions how they should sell the grid and this apply directly to the ownership unbundling conditions which is not yet legislation. So they take it as it is, although the member states and the Parliament has not accepted this legislative proposal, they think they can go forward. So this is completely upside down.” (Interview 2)

The third aspect is that of issue linkage. In fact, it could be argued that the Commission is “creating” the external conditions necessary for integration by using issue linkage. This seems to be the rationale behind the paper linking climate change and energy security issued right before the 2008 European Council. As an agenda setter this is a power that must not be underestimated. Still, ideological opposition voiced by Germany and other member states has the potential of creating backlashes to integration in line with Nye’s background conditions (Rosamond 2004: 72).

The theoretical approaches in this chapter have been used to show the complex nature of EU policy making. The idea has been to provide a comprehensive approach to European integration in the energy sector. The results have shown that even though there is evidence of spillover and loyalty shift, the situation is more unclear when searching with different tools. The approaches used have not been mutually exclusive, but rather they have highlighted the strengths and weaknesses of neofunctionalism. Some EU scholars advocate having different theoretical assumptions according to which level that is studied (Rosamond 2007: 127). In this perspective integration theories would serve the supersystemic level, institutionalist theories the systemic level and more actor oriented approaches the sectoral level (Ibid). This would limit the “grand integration theories” to only explaining history making arrangements, such as the Treaty reforms. This would not be sufficient for this purpose, which is why the approach here has been more encompassing. Rather than limiting the debate to a specific level, the theories have complemented each other, giving different perspectives to integration in the energy sector. The empirical richness of the EU energy sector has been systematised within different perspectives. Hopefully, the result is a comprehensive and balanced account as to how and why the Commission has gained influence in the energy sector. The study has unveiled a myriad of considerations that the Commission will not easily balance in the future. The EPE might be established, but the content is still far from defined.

7. Conclusion: The Commission as a powerful agenda setter under national scrutiny

This study has evaluated the role of the Commission as a driver for integration in the energy sector. Using historical development of EU competences it has been possible to detect the origins of the contemporary debate about EPE. The study reveals a great deal about the operation of the Commission as agenda setter. It is very persistent, and actively uses its existing powers to push integration. Furthermore it uses issue linkage actively to expand the scope of integration. The findings highlight the strengths and limits of the classical neofunctionalist approach. It is a comprehensive and applicable tool to assess the evidence of loyalty shift and spillover. Still, the EU is a complex institution, and contemporary approaches have been necessary to review the nature of the evidence more elegantly.

The empirical findings suggest a case for loyalty shifts in the energy sector, but it is modified by strong and persisting national ties. At the moment, member states and interest groups focus attention on the EU level for decision making. This has been illustrated by in both cases, firstly the bargaining over the Energy Package, and secondly on recognition of the Council for Commission policy proposals. In both cases, negotiations at the supranational level set the scene for further policy development. Still, the multi-level governance approach is in this respect a fruitful modification of the theory. Even if this study has revealed loyalty shifts, it does not exclude the option that governments and industry holds loyalties to several levels of government. This is surely the case here. National priorities in the German energy sector have given rise to strong resistance to legislative proposals in the internal energy sectors. Furthermore, member states are reluctant to give up the right to choose their own energy mix. This means that the loyalty shift is by now means total. This is strengthened by the fact that EU energy directives allow for flexible implementation of energy legislation, giving discretion to national priorities among

decision makers. Within the Commission there seem to be a coherent liberalisation ideological approach to supranational expansion of competencies. Still, organisational features of the Commission may create tensions between the national and supranational scope of authority in the case of external shocks.

The empirical findings strongly support the notion of the Commission as a driver of integration in the sector. It seems clear that the policy expansion has been initiated consistently by the Commission. This strengthens the notion for political spillover. The Commission has been acting as an entrepreneur of integrative ideas from the outset of European energy integration. The methods of issue linkage and “propose and concede” have been major contributions to establishing an Energy Policy for Europe. However, this would not be possible without sanctioning from the member states. This is why it has been interesting to contrast the work of the Commission with the strong opposition of Germany toward the Energy Package. Clearly, the persistence when facing strong opposition strengthens the case for the Commission as a driver of integration. Also in the second case member states have gradually surrendered competencies in line with Commission proposals. However, there have been some problems in linking the Internal Market as a general jurisdiction area of competencies to the issue specific nature of energy policy. This is a delicate concern for the Commission when establishing EPE.

There is a strong case for arguing that there has been a spillover from the Internal Market in the SEA into the energy sector. This can most clearly be seen in the *de jure* expansion of competencies for the EU in the energy sector. From being completely nationalised, the whole array of energy policy is now somehow covered by EU legislation. There has also been a spillover from the Internal Market to energy security. This leads me to conclude that there has been a political spillover under favourable external circumstances. There is no clear evidence of automatic spillover in this case. It could be argued that there is a functional link between internal and external security (Börzel: 2006). However, I would argue that external conditions play a greater role. The positive attitudes towards European integration in the post SEA-

era, the gas crisis and the fight against climate change were all conditions necessary to ignite integration in the energy sector. Furthermore, multi-level tiers of decision making and flexible implementation mechanisms modify the spillover effect, in that competencies are still partly resting at the national level. Also, integration has come easier in level than in scope. Again, national constraints call for flexible adoption and intergovernmental bargaining to reach EU positions.

Further research on this topic should expand the scope of actors. The role of the other EU institutions as integration drivers should be studied. This is especially true about the ECJ which has been progressive, but still underestimated in neofunctionalist reasoning (Schmitter 2004: 267) Furthermore, the European Parliament has expanded its competencies over the past four EU Treaties. It would be interesting to see if its role in the energy sector increases with the legal basis of the institution. Also, externalities deserve great attention. Externalities shape societies, and no political institutions remain unaffected. In this respect studies of resource scarceness and the impact of climate change would help to explain the pace of integration in the energy sector.

German resistance to the Energy Package clearly demonstrate the national sentiments are not obsolete in Europe. The EU of 2008 is a different place than the ECSC setting, but it is tempting to compare the statement of High Authority member René Mayer in 1956 to the contemporary debacle:

“There are many ways of defending power (...)Some consist of exercising them with vigour; others consists of not compromising them”
(Haas 1958: 469)

In 1956 the High Authority chose the second option (Haas 1958: 469). In 2008 the Commission exercise its power so vigorously that there member states might compromise them. The EPE is a proof that integration in the energy sector has reached far. Still, being a snapshot of history it is impossible to predict the outcome of energy integration. The energy power game is apparent but not yet settled.

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